AN ANALYSIS AND COMPARATIVE STUDY OF FINANCIAL STATEMENTS: THE CASE OF BREEZE BEACH CLUB AND VERACLUB (Z) LTD

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A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER IN BUSINESS ADMINISTRATION OF THE OPEN UNIVERSITY OF TANZANIA

2013

CERTIFICATION

I undersigned certifies that, I have read and hereby recommends for acceptance by the Open University Of Tanzania this research report titled **" An analysis and Comparative Study of Financial Statements", a case of Breeze Beach Hotel and Veraclub(Z) Ltd** in partial fulfilment of the requirements for the award of Master in Business Administration (MBA).

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Date

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DECLARATION

I **Mohammed, Salum Mansour** declare that the contents of this research report is the result of my own study and findings to the best of my knowledge, and that it has not been submitted for a similar degree in any other University.

…………………………………………….

Signature

…………………………………………….

Date

DEDICATION

This thesis is dedicated to my late father and family for their moral support throughout my studies. I also dedicate this to close friends, co-workers and academicians under the field of finance.

ABSTRACT

Financial statements are admittedly a storehouse of valuable information of the past performance and present position of business entities. They give an accurate picture of a company's condition and operating results in a condensed form. Accounting professional has been a major force over the years in shaping up financial statements. These financial statements prepared by accountants are normally prepared for general purpose. Any economic decision based on general purpose financial statements prepared by entities will not give appropriate results unless the financial statements should be analysed.

Analysis, comparability and interpretation of financial statements are necessary so that the difficulties behind these technical documents may be well understood and the real picture brought to light for the benefit of all concerned. Financial statements analyses help in determining the liquidity position, long term solvency, efficiency of using assets productively and profitability of a firm. Ratio analysis shows whether the company is improving or deteriorating in past years. Analysis of statements helps to determine the significance of the financial data.

The object of this study is to examine financial statements of the two hotels, Breeze Beach Club which is Non package hotel type and Veraclub Zanzibar which is Package hotel type. In this way it is possible to comment and comparing their financial performance and conditions by using financial ratios. Specifically, this study focuses on financial ratios to analyse profitability, liquidity, solvency, and

efficiency of using assets productively among the type of hotels. The financial statements of the two hotels for year 2008 to 2010 were the core source of data.

Based on these financial statements, the financial ratios were computed, interpreted, compared and thereafter results drawn. The results reveal that liquidity, efficiency and solvency ratios are favourable in Package hotel (Veraclub Zanzibar) compared with Non-package hotel (Breeze Beach Club). In terms of profitability both hotels are not well performed during the period of analysis.

The paper concludes by identify limitation on such analysis and provide suggestions for further analysis.

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LIST OF ABBREVIATIONS AND ACRONYMS

BBC	Breeze Beach Club
EBDIT	Earning Before Depreciation Interest and Tax
GDP	Gross Domestic Product
GP	Gross Profit
IFRS	International Financial Accounting Standards
NP	Net Profit
OCGS	Office of the Chief Government Statistician
SEC	Securities and Exchange Commission
TCCL	Tanga Cement Company Limited
TZS	Tanzanian Shillings
UNDP	United Nations Development Programme
USA	United States of America
USD	United State Dollar

CHAPTER ONE

1.0 INTRODUCTION

1.1 Background to the Study

Financial statements are formal records of the financial activities of a business, person, or other entity and provide an overview of a business or person's financial condition in both short and long term. They give an accurate picture of a company's condition and operating results in a condensed form. Financial statements are used as valuable information by different stakeholders in assessing the overall position and operating results of the company. For any financial decision, managers and stakeholders will need supporting information that helps to analyse and assess viability and profitability of a enterprise.

In order for financial information to be useful for various groups, they must be timely, relevant, reliable, understandable, and comparable. Under normal situation, financial information available to the majority of users is financial reports prepared annually by entities. In this case, financial reports are very crucial for various groups such as lenders, employees, investors and government agencies. The reports help them to analyse financial performance and position for decision making and planning.

More often, the financial reports prepared by entities contain financial and non financial matters. For financial matters, financial reports include financial statements that comprise income statement, balance sheet, and statement of total recognized

gains or lose, statement of cash flows and related schedules and notes. For non financial matters, financial reports include directors' reports and other information concerning the entity (example market strategies, financial planning). Unfortunately these financial statements, which are primarily prepared for general purpose, are not self sufficient for all users. Each party will be interested on different aspect of the entity's accounting and financial information. For example lenders will be interested in the entity's ability to meet its obligations (liquidity); shareholders will be interested in the firm's ability to pay dividends and increase the value of the firm's shares; tax authority will be interested in the firm's profitability (performance) and competitors will be concerned on financial strength or weakness of their rivals in order to take advantages.

Despite a fact that it is very expensive in terms of money and time for entities to prepare financial statements, yet few users understand well those documents. As indicated by McLaney (1997), to solve this problem the statements and information therein need further analysis and interpretation. When analyzed, the financial statements will provide more relevant, reliable, understandable and comparable sources of information on which different groups can use for decision making, as analysis makes financial complex figures simpler and understandable. A common tool available for financial analysis is "financial ratios". Financial ratios are the principal tools of analysing financial performance and positioning and they can be used by a variety of people to help diagnose the financial well-being of a firm.

The financial ratios are simplified forms of complex financial figures provided in the statements. The ratios are more easily understandable and comparable than financial

figures as they appear in statements. The financial ratio analysis, hence, enable the users to assess and evaluate firm's trading and financial soundness (profitability, liquidity, efficiency and leverage status) and therefore they are useful for making required economic decision. It also helps them to identify the trends that are developing and to gain more insight into the business.
The Hotel Industry is one of the major elements of tourism industry in Zanzibar. It is a major provider of employment to the society and is the main contributor to the government in terms of tax payments. Records show that the Hotel Industry (private sector) provides direct employment to 6,218 employees in 2009/10 earning about TZS 20,177 millions (OCGS, July 2011).

The Zanzibar Tourism Development Plan (UNDP, 1983) revealed that in that year there were only 10 unclassified accommodation units, providing 215 rooms and 467 beds. However, by 1990 there were 45 hotels and several establishments providing a total of 548 rooms and 1063 beds, which indicates an increase of 39 percent and 44 percent respectively. By the year 2000, the tourism sector has grown considerably and Zanzibar had 173 accommodation units under operation, which provided 6,159 beds. This marked an increase of 82.7 percent of bed capacity (Zanzibar Investment Policy, 2003). From year 2001 to 2011 additional accommodation units are estimated to be 195 providing 3,994 rooms and 7,419 beds (OCGS, 2011). In 2012 the accommodation units were expected to increase to 237.

The hotel industry seems to attract more investment into Zanzibar which will benefit the country. It is therefore essential to carefully study its financial condition and

worthiness. Unfortunately very limited work has been done in this area. This project is an attempt to analyze and interpret the financial statements of the two hotels. In this study two different hotels (Package and Non package hotel) are covered to analyse their accounting and financial information. The study will further comment on respective financial performance and business status using financial variables like liquidity, capital structures, while at the same time measure their risk and returns.

1.2 Statement of the Research Problem

Business entities are required by law to prepare financial statements showing their financial position and performance at specified period of time. As a rule, the accounting professional has been a major force over the years in shaping up financial statements. The financial statements that are prepared by accountants are normally for general purposes. Any economic decision based on such statements will not give appropriate results unless they are analysed. This is not because financial statements do not disclose all information necessary for everyone, but provide figures that are meaningless if they are not comparable, relevant, reliable, and understandable by different types of users.

When business entities prepare general purpose financial statements, there is a need for the general user, who becomes influenced with the numbers in the financial statements to get the real substance behind the numbers. Therefore, there is a reason for financial statements to be analysed in order to make economic decisions. This research intends to fill the gap by applying concepts of ratio analysis to interpret and compare the numbers shown in the financial statements of these two hotels. This will

provide users with relevant, comparable, reliable and understandable information relating to performance and position of the enterprises. All stakeholders will have the advantage of assessing enterprises liquidity, capital structures, and measuring risk and return.

1.3 Research Objectives

1.3.1 General Research Objective

To analyze, interpret and compare financial statements of two types of hotels so as to provide relevant, understandable, reliable and comparable information about the hotels' financial performance and conditions (strength or/weakness) by using financial ratios.

1.3.2 Specific Research Objectives

a) To determine the financial conditions and performances of selected hotels. The study will focus on financial ratios to analyse the profitability, liquidity, solvency, and efficiency of using assets productively among the type of hotels.
b) To analyse, interpret and compare selected financial ratios in order to provide the answers of how healthy are these hotels and which type is healthier than the other.

1.4. Research Questions

1.4.1 General Research Question

The general research question in this study is "How useful is it to analyse financial statements, compare and interpret them in such a way that they provide relevant,

reliable, understandable and comparable information to various stakeholders?"

1.4.2 Specific Research Questions

The following are the specific research questions for this study:

a) What is the trend of returns for each selected hotel by using profitability ratios and which hotel is in better positioned than another with respect to profitability?
b) What is the trend risk of each selected hotel by using liquidity ratios and which hotel is more risky than the other?
c) What is the trend risk of each selected hotel by using solvency ratios and which hotel is more risky than the other?
d) Which hotel is using its assets productively than the other?
e) Is there any similarity or diversion from the above ratios?

1.5 Relevance of the Study

This study is necessary so that the mystery behind the figures of financial statements may be revealed and the real picture brought to light for the benefit of several stakeholders. For examples, the potential investors will have the tools to make decision to invest on type of hotel which can maximise their wealth. The government can formulate policies which protect and improve tourism earnings/revenues in the country. The study also will help researchers to identify viable areas for further study. It may also be used as reference for researchers on finance and accounting. More specifically this study is done to enable the researcher to fulfil the requirement for the Master Degree of Business Administration of the Open University of Tanzania.

1.6 Limitations of the Research

During the period of research process the following constraints are expected which may limit an in-depth study and analysis:

a) Inherent limitations of the accounting data and the ratios themselves.

b) Financial statements were used more extensively as they were enough to provide the required information for analysis.

c) Lack of research centre in this country will limit a researcher to obtain some information very relevant to this study. However, the researcher will use internet to search for reliable information (professional journals, e-books and so on) to make this study comprehensive.

d) Financial statements were presented in different currencies. However, for comparability purposes the researcher used United State Dollar as a common currency.

1.7 Organisation of the Study

Chapter one describes main parts of the thesis such as background to the study, statement of the research problem, research objectives, research questions and relevance of the study. In the next chapter, the report covers literature review while chapter three covers research design and methodology. In chapter four, the report discusses the findings followed by the Conclusion and recommendations are provided in chapter five.

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter gives the critical review of the relevant literature findings concerning the study. Conceptual definitions that are applied in the study are given under the first section while section two describes supporting theories. The third section concentrates on the empirical analysis of the study and section four identifies the research gap between theoretical and empirical literatures. Section five illustrates the framework of the study and related variables while the sixth section covers the characteristics of the variables within the model. The last section is a summary of the important aspects in this chapter.

2.2 Conceptual Definition

Due to its importance financial statement analysis has become very common in most of the accounting and finance literature. McMenami (1999) defines financial analysis as “the evaluation of a firm’s past, present and anticipated future financial performance and financial condition”. Its objectives are to identify the firm's financial strengths and weaknesses and to provide the essential foundation for financial decision-making and planning.

On another angle**,** financial statement analysis refers to an essential first step towards gaining a sound understanding of a business (one's own or a competitor's) - its financial strengths and weaknesses, its financial opportunities and risks (McMenami, 1999).

Another writer, Pandey (1998, p.103) defines financial analysis as the process of identifying the financial strengths and weaknesses of the firm by properly establishing relationships between the items of the balance sheet and the profit and loss account. Financial analysis can be undertaken by management of the firm, or by parties outside the firm (example, owners, creditors, investors and others**.**

The term financial analysis is also known as "financial statement analysis or accounting analysis", which refers to an assessment of the viability, stability and profitability of a business, sub – business or project (Pandey, 1998).

The key concept is that financial analysis is a process whereby an analyst employs various tools such as financial ratios to translate complex accounting data of financial statements in order to provide more relevant, reliable, understandable and comparable sources of information to which various groups can use for economic decision making.

In order to conduct financial analysis, financial ratios are used. In simple terms, financial ratios are defined as the principal tools of financial analysis and they can be used by a variety of people to help diagnose the financial well-being of a firm (McMenami, 1999). According to Kim (2006, pp95-106), the main input of financial ratios is financial statements. The financial statements are defined as structured representation of the financial position and financial performance of an entity (IFRS 2004). The financial statements include a) statement of financial positions; b) statement of comprehensive income; c) statement of changes in equity; d) statement

of cash flows; and e) notes to the schedule attached to the financial statements. These are explained hereunder:

a) Statement of financial position/Balance sheet

Statement of financial position or Balance Sheet is defined as a statement that describes the financial condition or the state of affairs of a business at a particular moment in time. Statement of financial position or balance sheet contains the following aspects: - The Current Assets, Non current Assets, Current Liabilities, and non Current Liabilities, and Reserve. The main functions of statement of financial position/Balance sheet are: a) to give a concise summary of the firm's resources, obligations and owners' equity; b) provides a measure of the firm's liquidity; and c) a measure of the firm's solvency (IFRS 2004).

b) Statement of comprehensive income/ Profit and loss account

The income statement presents a summary of the revenues, gains, expenses, losses, and net income or net loss of an entity for a specific period. It shows results of operations during a given period of time (usually a year). The main function of a statement of comprehensive income is to give a measure of the firm's profitability and provides a concise summary of the firm's revenues and expenses during a given per (IFRS 2004).

c) Statement of owner's equity

A statement of changes in equity is an important component of financial statements since it explains the composition of equity and how has it changed over the year.

Typical information we can get from a statement of owner’s equity include items of income and expenses recognized in income statement for the period, the amount of new share capital issues, the effects of changes in accounting policies, corrections of errors recognized in the period, and the amounts of investments by, and dividends and other distributions to equity investors during the period (IFRS 2004).

d) Cash flow Statement / Statement of cash flow for the period

The cash flow statement summarizes a business's cash receipts and cash payments relating to its operating, investing, and financing activities during a particular period (IFRS 2004).

e) Notes and schedule accompanying financial statements

The notes and schedule present information about the basis of preparation of the financial statements and the specific accounting policies used (IFRS 2004).

2.3 A Review of Supporting Theories

2.3.1 General Overview

Communication on the activities, progress and future plans of any enterprises between management and shareholders or other stakeholders is through the annual reports and accounts (Holmes et al.2002) as sighted by bakari (2008).The most important contents of the annual report are Director’s Report, Profit and Loss Account, Balance sheet and Auditors’ report. These are all contained in the financial statements for the purpose of informing all concerned parties about the company’s activities. However, a summary of financial statements, as is published in the reports,

does not contain sufficient information to allow a full understanding of the results and state of affairs of the firm (McLaney, 1997). In this respect it is important to perform a financial analysis and thereafter interpret findings.

Any business will not flourish without sound financial planning. This activity is possible where financial information provided is accurate and timely. Management and Shareholders use the financial information in order to predict, compare and evaluate the firm's earnings ability. This information has to be analysed so that an ordinary person can make sense on the data and be able to appraise the performance of a company. As such it is an essential first step towards gaining a sound understanding of a business by evaluating its financial strengths and weakness, its financial opportunities and risks.

2.3.2 Authority of Financial Statements

According to Kiligane (2000, pp 211) authorities on financial statement for enterprises operating in the country, which are intended to provide financial information to interested parties, derive authority from the followings organs: - a) Accounting standards and Guidelines issued by the National Board of Accountants and Auditors (NBAA); b) Companies Ordinance Cap 212; c) Specific Acts of incorporation-this was particularly the case during the centrally controlled economy era.

Most companies falling under this category are being phased out. Typically companies that were falling under Public Corporations Act 1969 of United Republic

of Tanzania as amended in 1992; d) Regulatory Agencies like the Bank of Tanzania for banks and financial institutions, Capital Market and Securities Authority for public issues of financial instruments, and Commissioner for Insurance.

2.3.3 A Framework for Financial analysis

According to writer McMenamin(1999, p. 298) described that to gain an understanding of a firm's financial position and performance(financial analysis) is essentially seek to find answers to four key questions which he used to develop a general framework for financial analysis. The key questions are as follows:

a) Is this business making money, that is, is it profitable?
b) Can this business pay its bills on time, that is, is it liquid?
c) Is this business using its assets productively, that is, is it operating efficiently?
d) Is this business overly dependent on borrowed money, that is, is it too highly
e) geared?

2.3.4 Financial Ratio

Evidence exists that since the late 1800’s ratio analysis has been widely used in the study of published financial data. Indeed, ratios have been used to help evaluate companies’ financial condition since the beginning of the finance discipline (Lawder, 1989). Literature on financial statement analysis discusses the use of ratio analysis as a fundamental tool for evaluating the financial health of a company, and many financial ratios have been developed and are used by practitioners and academicians. Moreover, accounting and finance textbooks typically emphasize the use of ratio analysis.

Due to the importance of “Financial Ratios” in financial analysis, several parties, such as accountants, analysts, bankers, managers, investors and owners, use these ratios as a main tool to help evaluate a firm's financial performance and financial condition and to compare these with other like firms or with itself over time. Profitability ratios, for example, measure financial performance, whereas liquidity ratios measure financial condition. It is important to remember that financial analysis is much more than a number-crunching exercise. It requires interpretative skills to assess future strategic potential as well as evaluating past performance (McMenami 1999, pp 298).

2.3.5 Nature of Ratio Analysis

In financial analysis, a ratio is used as a benchmark for evaluating the financial position and performance of a firm. The absolute accounting figures reported in the financial statements do not provide a meaningful understanding of the performance and financial position of a firm. Accounting figures convey a meaning when it is related to some other relevant information. Ratios help to summarise the large quantities of financial data and to make qualitative judgement about the firm’s financial performance (Pandey1998, pp 104).

If a certain company states that its profit is TZS 10 million from sales of TZS 100 million or 10 percent net profit margin; such information is meaningless to the user because it does not provide sound judgement on whether this profit is favourable or not. The only information which can lead to judge whether this profit is favourable or not is to compare with other ratios. Therefore, a meaningful basis for comparison is

necessary in order to answer the question such as “Is it bad or good?” or “Is it too high or low”? In this sense the nature of financial ratios should be compared with other ratios.

2.3.6 Standard of Comparison

The ratio analysis involves comparison for a useful interpretation of the financial statements. A single ratio in itself does not indicate favourable or unfavourable condition. It should be compared with some standard. The standard of comparison may consist past ratios, projected ratios, competitor’s ratios and industry ratios (Pandey 1998, pp 104-5). On the other hand, Gitman (2007) mentioned two common types of comparative financial ratio which are Cross-section analysis and Time series/trend analysis. These are explained hereunder:-

i. Cross-sectional analysis involves a comparison of different firms’ financial ratios at the same point in time. Analysts are often interested in how well a firm has performed in relation to other firms in its industry at a given time. Frequently, a firm will compare its ratio values to those of a key competitor or group of competitors that it wishes to emulate. This type of cross-sectional analysis which is also called benchmarking has become very popular (Gitman 2007, pp 50).

ii. Time-series analysis evaluates performance over time. Comparison of current to past performance, using ratios, enables analysts to assess the firm’s progress. Developing trends can be seen by using multiyear comparisons. As in cross sectional analysis, any significant year-to-year changes may be symptomatic of a major problem.

The most informative approach to this study will combine both cross-sectional and time-series analysis. The main obstacle of time series is the volume of data over time and the technicalities of computing.

2.3.7 Types of Ratios

Several ratios, calculated from the accounting data, can be grouped into various classes according to financial activity or function to be evaluated. Singh and Schmidall (2006) arranged the financial ratios into five categories based on their purpose. These five categories are based on specific purpose such as liquidity, efficiency, leverage, solvency, and profitability ratios. An additional sixth category that is an operating ratio, is included to assist management in analyzing the operations of an establishment (Fong Kah Seng 2001, pp.14). From the total of five categories of ratios, several sub-categorical financial ratios are chosen to do the financial analysis in this study. The purpose of these ratios is explained hereunder:

i) Liquidity ratios – This is measure the firm's ability to meet current obligations.

ii) Activity ratios- Reflect the firm's efficiency in utilising its assets.

iii) Leverage ratios - Measures the degree a company is relying upon debt financing.

iv) Solvency ratio – Measures the degree of debt financing and ability to pay long-term financing obligations.

v) Profitability ratios- Measure overall performance and effectiveness of the firm.

vi) Operating ratio- Measure management's efficiency in regards to its operation.

2.3.8 Importance of Financial Ratios

Writers attach great importance to financial ratios for assessing the healthy of a company and make economic decision. For example, financial ratio provides an efficient means by which financial data can be reduced to an understandable basis for evaluation of financial conditions and operating performance. According to Kennedy (n.d) several researchers such as Altman, 1968; Beaver, 1966; Daniel, 1969; Deakin, 1972; and Horrigan, 1966 have written the importance of financial ratio and concluded that financial ratios have predictive ability. Predictive ability is measured by determining the statistical predictive relationship between financial ratios and some specified real world phenomenon, for example, bankruptcy (Altman, 1968), business failure (Beaver 1966, Daniel 1969 and Deakin 1972) and long-term credit standing (Horrigan 1966) as sighted by Kennedy. This means that financial ratios can be used to predict business failure or success for any type of enterprise. This helps investors and other groups (lenders, creditors) to decide where to put their money for wealth maximization. The analytical capabilities of ratio analysis has an important place in assessing an organization's current financial status, establishing measures for future strategies and tasks to accomplish its mission, evaluating its performance over time, and deciding how the organization should proceed in the future (Abraham, 2006).

2.4 Empirical Analysis of Relevant Studies

This section provides selected practical studies of empirical analysis based on Tanzania experience and elsewhere on Analysis and Comparable Study of Financial Statements.

2.4.1 Experience from Other countries.

Said (2003), in his report analysed and compared the Financial Statements of two Telecommunication Companies, namely The Bell Canada Enterprises Group of Canada and The BellSouth Corporation Group of the USA, for the purpose of commenting on their investment worthiness. In order to assess them, he used the published Financial Statements of the two groups and analysed their return history, risk of their investments, dividends policies used, investment policies used, type of financing employed and their capital structure. He also applied different methods (example book value method, income statement based-method, price earning ratio method) to calculate the value of these companies and finally he performed the ratio analysis techniques to arrive to his conclusion for his study.

The results of his study show that both groups are faced with stiff competition in the industry; however, their managements are working hard to cope with this situation for the future prospects to look good. In terms of financially positioning, he concluded that they are all healthy and opportunities are available in telecommunications industry, despite the type of risk faced by both. But proper policies and strategies supported by a strong management team (that seem both groups to have) with a long term vision can help to exploit fully the available opportunities for an effective competition and success.

2.4.2 Review of Relevant Studies in Tanzania

Bakari (2008), in his research report analysed and interpreted financial information contained in annually financial statements published by Tanga Cement Company

Ltd. The purpose of his study was to gain relevant and reliable information about the company's trading and financial strength or/ weakness. The data used in his analysis was obtained from annual financial reports for five years from 2001-2005. The techniques/methods used to analyze and interpret the financial statements were the combination of Ratio analysis and the Trend analysis or time series technique. All major groups of ratios (Profitability, Liquidity, Efficiency, Gearing and Investment) were involved in his study. He measured performance of Tanga Cement Company Ltd by using Gross Profit Margin ratio, Operating Profit Margin, and Net Profit Margin ratio. The results were as follows:-

Table 1: TCCL Gross Profit Margin

Years	**2001**	**2002**	**2003**	**2004**	**2005**
Gross Profit Tsh "000"	7,048,760	12,113,545	14,502,127	14,899,644	16,932,773
Gross Profit (GP) %	24	30	28	27	25

Source: Bakari (2008)

The ratios above show that gross profit increased from year 2001-2002, then from the year 2003-2005 dropped. The main reason for the drop in gross profit margin was due to increased in cost of goods produced (unit of product). The average spread between the cost of goods produced and sales revenue for the period of 5 years is 26.8%. These results reflect the efficiency of management in producing a unit of product at lower cost.

Table 2: TCCL Operating Profit Margin

Years	2001	2002	2003	2004	2005
Operating Profit TZS "000"	3,040,550	7,724,977	10,020,257	9,387,674	10,560,361
Operating Profit %	11	19	19	17	16

Source:Bakari (2008)

The Operating Profit Ratios shown above increased from the year 2001 to 2003. However, in the year 2004 to 2005 the ratios dropped to 16% from 19% in 2003. This decrease of operating profit in year 2004 was mainly caused by increased in sells plus administration expenses.

Table 3: TCCL Net Profit after Tax

Years	2001	2002	2003	2004	2005
Net profit (after tax) Tsh "000"	1,961,038	4,679,858	6,377,491	6,516,959	7,233,041
Net Profit (%)	7	12	12	12	11

Source:Bakari (2008)

The net profit margin increased from 2001 to 2002 and then from 2002 to 2004 was stabilised until the year 2005 where it dropped to 11%. The declined in net profit in the year 2005 was caused by an increased amount of tax paid, selling and administration expenses.

In his study, he also measured financial position of Tanga Cement Company Ltd by computing liquidity ratios. The results of liquidity ratios are explain below:-

Table 4: TCCL Liquidity Ratio

Years	2001	2002	2003	2004	2005
Current Ratio	1.85:1	2.39:1	2.69:1	3.81:1	1.55:1
Quick Ratio	0.95:1	1.67:1	1.81:1	1.93:1	0.59:1

Source:Bakari (2008)

The current ratio was calculated by dividing current assets by current liabilities. The ratio indicates that there was an increase of current assets over current liabilities from the year 2001 to 2004. However, in the year 2005 the current ratio decreased. This decreased caused by increase in current liabilities in the year 2005. The trend of current ratios show that at any year from 2001-2005 the company was in a good position to meet its current obligations which is very important for any business.

The quick ratio established a relationship between quick or liquid assets and current liabilities. The quick ratio of Tanga Cement Company Ltd shows that it increased from 2001 to 2004; in 2005 the quick ratio decreased as a result of growing current liabilities. Generally a quick ratio of 1 to 1 is considered to represent a satisfactory current financial position. This means that in the year 2001 and 2005 the company could not pay its entire current obligation immediately even if it was forced to do so.

In general, the above analysis indicates that earning capacity, ability to pay debts and other obligations on time, ability to survive and prosper are favourable. From these results, then the researcher concluded that Tanga Cement Company Ltd is improving its performance every year which is desirable for existing shareholders and may

attract prospective investors in the company. However, the researcher could not compare those ratios obtained in his study with other companies or industry averages ratio to make the study more meaningful.

2.4.3 Review of General Studies

Volker et al (2001) in their study analysed and evaluated the cross-sectional variations of financial ratios among different sizes of private companies. The study analysed the retail and service sectors over the period from 1998 to 2000 by examining four ratio categories. The ratio categories include: (1) liquidity, (2) activity, (3) leverage, and (4) profitability. Results provide strong evidence that small retail firms perform differently than larger retail firms in all categories and different time periods. Service firms had the strongest and most consistent differences in activity and profitability ratios. Separate comparisons of the retail and service sectors also showed significant performance differences in every ratio category.

2.5 Research Gap Identified

Several researches and literature show the importance of analysing financial statements by using financial ratios as a tool in appraising performance and business condition. For example Dong Jim Kim (2006, p.95) in his study says that "investors and financial analysts have long been using financial ratios in order to evaluate companies' financial performance and conditions". However, there is little or lack of knowledge on financial analysis to the public which cause many enterprises to be misled by management on assessing performance and positioning of the business concerned. All available information regarding operation of hotels does not contain

detail technical analysis and hence policy and decision makers cannot make sound judgement regarding levels of profitability. In this regard calculations on tax liability are distorted. Therefore, there is need to conduct financial analysis for hotel industry in Zanzibar to be analysed and determine their financial strength and weakness within themselves or by comparing from each other.

2.6 Analytical/Conceptual Framework (For Studying the Problem and Analysing The Data)

Financial ratios are the main diagnostic tools of financial analysis. They are used to evaluate a firm's financial health, performance and to check its financial vital signs. In general this study will analyse and relate the variable that may indicate whether one of the hotels is in favourable financial performance or condition than the other hotel. Some of those variables are summarized in Table 5 below:

Table 5: List of Variables

Independent Variables	Dependent Variables	Outcomes
Profitability Ratios 1. Gross Margin ratio 2. Net Profit Margin ratio 3. Earning Before Depreciation Interest and Tax(EBDIT)	Measurement of performance	Higher ratio indicates good performance
Liquidity Ratio 1. Current ratio 2. Quick ratio 3. Cash ratio	Measurement of Risk	Higher ratio indicates good position
Activity Ratio 1. Inventory turnover 2. Debtors turnover 3. Assets turnover	Measure of Efficiency	Higher ratio means good performance
Leverage/Solvency Ratios 1. Total debt ratio 2. Debt-equity ratio	Measurement of capital structure	Higher ratio indicates more risk or high risk

Source:Fieldwork

2.7 Theoretical Framework

Financial ratio analysis formalizes and quantifies financial data to facilitate comparison within an organization (Abraham 2006, pp 2). It is an excellent method for determining the overall financial performance and condition of a hotel's business. According to Dennis (2006), as sighted by Seng(2001), financial ratios are also useful for making comparisons between a customer and other businesses in an industry (Fong Kah Seng 2001, pp 17).

It is expected that when the financial statements of two companies are analysed by computing various ratios, interpreting them and comparing from one company to another, then the meaningful of analysis and comparable study will be obtained. The following are the financial ratios' formulas and their explanation in the financial analysis. These are also the variables that will be measured.

Brief Explanation of Ratios

Profitability Ratios

Profitability ratios measure the results of business operations or overall performance and effectiveness of the firm (http://www.accounting4management.com)[Accessed on 5 March 2012]. Perhaps the types of ratios most often used and considered by those outside a firm are the profitability ratios. Profitability ratios provide measures of profit performance that serve to evaluate the periodic financial success of a firm.

Return on sales reveals the profits earned per dollar of sales and therefore measures the efficiency of the operation and is an indicator of the ability to withstand falling prices, rising costs and declining sales. Return on net worth (return on equity) is used

to analyze the ability of the firm's management to realize an adequate return on the capital invested by the owners of the firm.

Table 6: Summary of financial ratios formulas will be used in this study

Ratio Category	**Ratio**	**Formula**
Profitability	Gross Margin Ratio	Gross Profit
		Sales
	Net Margin	Profit after Tax
		Sales
	EBDIT	EBDIT
		Revenue
Liquidity	Current Ratio	Current assets
		Current liabilities
	Quick Ratio	Current assets-Inventory
		Current liabilities
	Cash Ratio	Cash +Market securities
		Current liabilities
Ratio Category	**Ratio**	**Formula**
Activity	Inventory turnover	sales Inventory
	Debtors turnover	Credit sales or sales
		Debtors
	Assets turnover	Sales
		Net assets
Leverage	Total debt	Total debt
		Capital employed
	Debt-equity	Net worth
		Total debt

Source: Fieldwork

Gross Profit ratio

The gross profit ratio indicates the relation between production cost and sales and efficiency with which the goods are produced or purchased. A high gross profit ratio may indicate that the organization is able to produce or purchase at a relatively lower cost (Ketan, 2007).

Net Profit ratio

The net profit ratio indicates that portion of sales available to the owners after the consideration of all types of expenses and costs either operating or non operating or normal or abnormal. A high net profit ratio indicates higher profitability of the business (ketan, 2007).

The EBDIT to revenue explains the profitability strength of earnings before depreciation, interest and tax to revenue. It is the profit earned from the business before consideration of depreciation, interest and taxes. The higher the ratio, the stronger is the profitability of the business.

Liquidity Ratios

The liquidity ratio measures the ability of an entity to meet its current and short-term obligations (Schmidgall, 2006). These ratios are calculated to comment upon the short term paying capacity of a concern or the firm's ability to meet its current obligations. The majority of the guests settle their hotel stay or any services provided by hotel to the guests by using credit cards which take some time until delivered to the bank. At the same time the hotel needs to pay its bills to various suppliers.

Therefore, the liquidity ratio shows the hotel’s ability to meet its short term obligations and whether a company can pay its bills on time, which are important considerations for managers and unsecured trade creditors.

The current ratio formula is current assets divided by current liabilities. It is one of the best-known measures of financial liquidity and is the standard measure of the business's financial health. It will also give an indication whether a customer is able to meet its current obligations by measuring if it has enough assets to cover its liabilities.

In the hospitality industry, the largest inventories held by a hotel operation are in the number of guest rooms available for sale and these are included under “building”. This is part of fixed assets that is included in property, plant, and equipment (Jagels, 2007). The current inventories held for resale are for food and beverage services, but these current inventories represent only a small portion of current assets. Therefore, hotels can operate with a current ratio of 1.5 or less (Jagels, 2007). The quick ratio is better accepted in the hotel industry as a liquidity ratio and as a more stringent test as it only considers cash and near cash assets (Schmidgall, 2006). In most segments of the hospitality industry based on the small amounts and fast turnover of inventories, the industry average is less than 1 to for the quick ratio.

The quick ratio is a more rigorous measure of liquidity because it excludes inventories when evaluating current assets. It only takes into account current assets to current liabilities that are cash and can be converted to cash within a 0 to 90 day

period. The quick ratio focuses on cash and accounts receivable because these cash assets can be converted into cash quickly. Creditors, owners, and managers analyze and interpret the quick ratio the same way they analyze and interpret the current ratio. While creditors prefer to see a high ratio, owners prefer a low ratio. This means management must maintain a balance between the creditors' and owners' viewpoints (Jagels, 2007).

Activity Ratio

Activity ratios are calculated to measure the efficiency with which the resources of a firm have been employed (http://www.accounting4management.com) [Accessed on5 March 2012]. These ratios are also called turnover ratios because they indicate the speed with which assets are being turned over into sales (Pandey1998, pp 117).

Asset utilization ratios (Activity ratios) provide measures of management effectiveness. These ratios serve as a guide to critical factors concerning the use of the firm's assets, inventory, and accounts receivable collections in day-to-day operations. Asset utilization ratios are especially important for internal monitoring on the performance over multiple periods. It serves as warning signals or benchmarks from which meaningful conclusions may be reached on operational issues.

Inventory turnover

A high inventory turnover ratio indicates that maximum sales turnover is achieved with the minimum investment in inventory. As such as a general rule, high inventory turnover ratio is desirable.

Leverage Ratios

Leverage ratios, also known as capitalization ratios, provide measures of the firm's use of debt financing. These are extremely important for potential creditors, who are concerned with the firm's ability to generate the cash flow necessary to make interest payments on outstanding debt. Thus, these ratios are used extensively by analysts outside the firm to make decisions concerning the provision of new credit or the extension of existing credit arrangements. The short-term creditors, like bankers and suppliers of raw materials are more concerned with the firm's current debt-paying ability while long term creditors are more concerned with the firm's long term financial strength (Pandey 1998, pp 111).

Debt-equity ratio indicates the state of shareholders or owners in the organization vis-à-vis that of the creditors. It indicates the cushion available to the creditors on liquidation of the organization. A high debt-equity ratio may indicate that financial status of the creditors is more than that of the owners. A very high debt-equity ratio may make the proportion of investment in the organization a risky one. On the other hand, a very low debt equity rate may mean that the borrowing capacity of the organization is being underutilized (ketan, 2007).

Debt Ratio is defined as "the percentage of funds provided by current liabilities and long-term debt. Creditors prefer low debt ratios because the lower ratio, the greater the cushion against creditors' losses in the event of liquidation. Stockholders, on the other hand, may want more leverage because it magnifies expected earnings.(Kovo 2010, pg 28).

2.8 Summary

The discussion in this chapter provides a very brief critical review of the relevant literature findings concerning the analysis of financial accounting data. A highlight on the material facts on the topic and related to the study is also given.

Financial analysis is defined as the process of identifying the financial strengths and weaknesses of the firm. The analysis necessitates the need for properly establishing relationships between the items of the balance sheet and the profit and loss account. The objectives are therefore to identify the firm’s financial strengths and weaknesses, thereafter provide the essential foundation for financial decision-making and planning.

In order to conduct financial analysis, financial ratios are used. Financial ratios are the principal tools of financial analysis and they can be used by a variety of people to help in diagnosing the financial well-being of a firm. The main input of financial ratios is financial statements which include a) statement of financial position; b) statement of comprehensive income; c) statement of change in equity; d) statements of cash flows; and e) notes to the schedule accompany the financial statements.

The most important financial dimensions which a firm is likely to analyze are: liquidity, activity ratio, leverage ratio, solvency, profitability and operating ratio. Liquidity ratios measure the firm’s ability to meet current obligations while activity ratios reflect the firm’s efficiency in utilising its assets. On the other hand, leverage ratios measure the degree a company is relying upon debt financing.

A very important ratio in checking the sustainability of firm is solvency ratio. It measures the degree of debt financing and ability to pay long-term financing obligations. On the other hand, profitability ratios measure overall performance and effectiveness of the firm. Operating ratio measure management's efficiency in regards to its operation.

CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Overview

This chapter illustrates the research method was used in data collection, measurement and analysis and the reason behind the choice of the method. This is a conceptual structure within which the research is conducted; it constitutes the blueprint for the collections, measurement and analysis of data (Kothari, 1990).

The intention of this research is not to take responsible position on any hotel used in this study as an expert of analysing the numbers, but the desire is to analyse and compare financial information of these two hotels based on knowledge, skills and information acquired.

3.2 Research Strategies

The research design in this study is “case study”, being descriptive in nature which was carried out by analysing financial statements of the two hotels by using financial ratios. Descriptive approach is used in the theoretical part so to give descriptions of the various important concepts such as financial statement analysis, comparability and financial ratio. Description of these important concepts will serve as the basis for the empirical study. In addition to this approach, explanatory approach was used, which will in turn help to interpret results from the analysis of financial statements.

The financial ratios are selected as a tool for financial analysis because they are principal tools in this field and can be used by a variety of people to help diagnose

the financial well-being of a firm. The nature of this study will not firmly demand use of primary data. However, primary data (questionnaire) was used to get more information which can not directly be obtained from the financial statements. Therefore, the financial statements were core data sources for this study.

3.3 Survey Population and Sampling

According to directory of Zanzibar Commission for Tourism, Zanzibar has 237 hotels that include package and non-package hotel (www.zanzibartourist.net). The main approach to select hotels for analysis was to select 2 hotels that operate as Package hotel and Non Package hotel to study their respective financial statements for the period of three years from 2008-2010 as shown in (Appendix III and IV). In addition to that, these hotels should have same financial period and almost identical capacity in terms of number of rooms. These financial statements used are obtained directly from the hotels themselves. The decision to select only two hotels is based on time constraint; furthermore, the analysis is for individual hotels and does not aim to represent the whole industry at large. Therefore, these samples are enough to meet the purpose of this research.

3.4 Area of Research or Survey

The study was conducted in the Island of Unguja (Zanzibar) where both hotels are operating their businesses. The researcher purposely chooses this area because hotels business has grown enormously in Zanzibar and surrounding region since 1985 after business and trade liberation policy followed by enactment of Investment Promotion legal framework.

3.5 Methods of Data Collection

Data collection is very essential to any research. Through this process, researcher accumulates empirical material to support their findings. There are two main types of data collection methods; primary and secondary. The primary data collection method is about creating new data by using questionnaires and carrying out interviews. The secondary data collection method is about collecting and analyzing existing data. This study employs both methods of collecting data in order to be well-suited with the analysis. However, secondary data collecting method is most suited to this study. These are in the form of published audited financial statements obtained from Registrar of Companies or from hotels themselves, available literature and website. Most useful documents are statement of financial position, statement of comprehensive income, statement of changes in equity, statements of cash flows and notes and schedule accompany with financial statements. Information derived was used to compute several financial ratios as shown in (Appendix V and VI) which are in line with the objectives of this research. In addition, questionnaires were used in order to obtain information which contributes technically to interpret the financial ratios while interview or discussions were used to obtain companies' profile. The research questions were tested by using several ratios and other documentary information. The results of this analysis will eventually lead to make a number of observations and thereafter suggest useful recommendations.

3.6 Data Processing and Analysis

According to Kothari (1990) Data Processing implies editing, coding, classification and tabulation of collected data so that they are amenable to analysis. It is a process

that prepares collected raw data and paves a way for a smooth analysis (Adam J 2007, pp 122). In this study, manual editing and tabulation of processed data were carried out. Editing is continuous process of examining the collected raw-data in order to detect errors and omissions and thereafter make appropriate corrections. Tabulation was used as a process of summarising collected raw data and displaying them in compact form (statistical tables) so that they can be easily analysed (Adam J 2007, pp 127). Data from documentary review were organized into manageable units through simple hand coding to facilitate data analysis. It is true that financial analysis means thorough explanation of each received result.

The computations and analysis was done using Microsoft Excel based on formulas presented in chapter two. There are many advantages of this approach such as convenience, stability and popularity of the software and relative accessibility (or easiness of use). The results were summarised by using tables and charts. For best data processing, editing and coding the necessary information, both qualitative and quantitative methods were used.

Quantitative method is used to analyze data derived from numbers collected from numerical and standardized records. Using this method, the numerical data were analyzed through statistical methods. In this case, tables and charts were employed to reveal some important characteristics of the selected samples. A qualitative method is used for non-standardized data. The interpretation and meanings are expressed through words. A researcher employ this method at the time of giving comments on the information obtained. Through this process, it is possible to establish relation

between variables which involve the use of percentages, tables and charts to reveal some important characteristics of the study for selected samples.

CHAPTER FOUR

4.0 RESEARCH FINDINGS AND ANALYSIS

4.1 Overview

This study analysed and compared financial statements of two different types of hotel, namely Breeze Beach Club which is non package hotel type and Veraclub Zanzibar which is package hotel type, in order to evaluate their financial condition and performance. Published financial statements of the two hotels for three years (2008 to 2010) and ratio analysis techniques have been applied as main tools of analyzing the financial statements. The study demanded use of secondary data, that is financial statements of the two hotels. In addition, questionnaires were used to collect some information which contributes technically to interpret the financial ratios. The questionnaires were distributed to financial controllers of the two hotels and all responded positively; that is 100 percent response rate.

The research findings are categorized in two parts. Part A involved evaluation of the financial conditions and performance of each hotel over time while Part B involved comparison between two hotels. The financial ratios obtained from the analysis have been summarized in tables 7 to 14 below. Graphs (figure 1 to 33) are also used as a means to portray some important characteristics of the results.

4.2 Analysis and Interpretation of the Findings

The research findings are presented in the form of time-series for each hotel as individual and cross-sectional analysis will compare two hotels. The following are results:-

4.3. Time Series Analysis of Breezes Beach Club

4.3.1 Profitability Ratios

Profitability ratios replicate the results of all areas of management's responsibilities (Schmidgall, 2006). Table 7 below represents profitability ratios for Breezes Beach Club.

Table 7: Profitability Ratios of Breezes Beach Club

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Profitability	Gross Profit Margin	80 percent	76 percent	77 percent
	Net Profit Margin	-6 percent	-24 percent	-13 percent
	Earning Before Depreciation Interest and Tax(EBDIT)	15 percent	3 percent	13 percent

Source:Field work

i) The Gross Profit Margin Ratio

The gross profit margin ratio shows profit relative to sales after the deduction of production cost, and indicates the relation between production costs and selling price. Figure 1 below shows gross profit margin of Breezes Beach Club. It shows how much the amount of sales is left (after cost of sales) to absorb non-production or administrative costs. The time-series analysis indicates that the hotel left 80 percent, 76 percent and 77 percent of revenue in 2008, 2009, and 2010 in respective years for administrative and other operating costs. The trend also shows that in the year 2008 the hotel performed better by improving its revenue compared to the year 2009 when revenue dropped by 28 percent. It is possible that this slow down of revenue in the year 2009 was caused by global financial crisis that hit the hotel industry. In year 2010, the hotel had gross profit margin of 77 percent indicating a slight increase from

76 in the year 2009. It is possible that the global financial crisis still had an impact on the hotel but not much as in the year 2009.

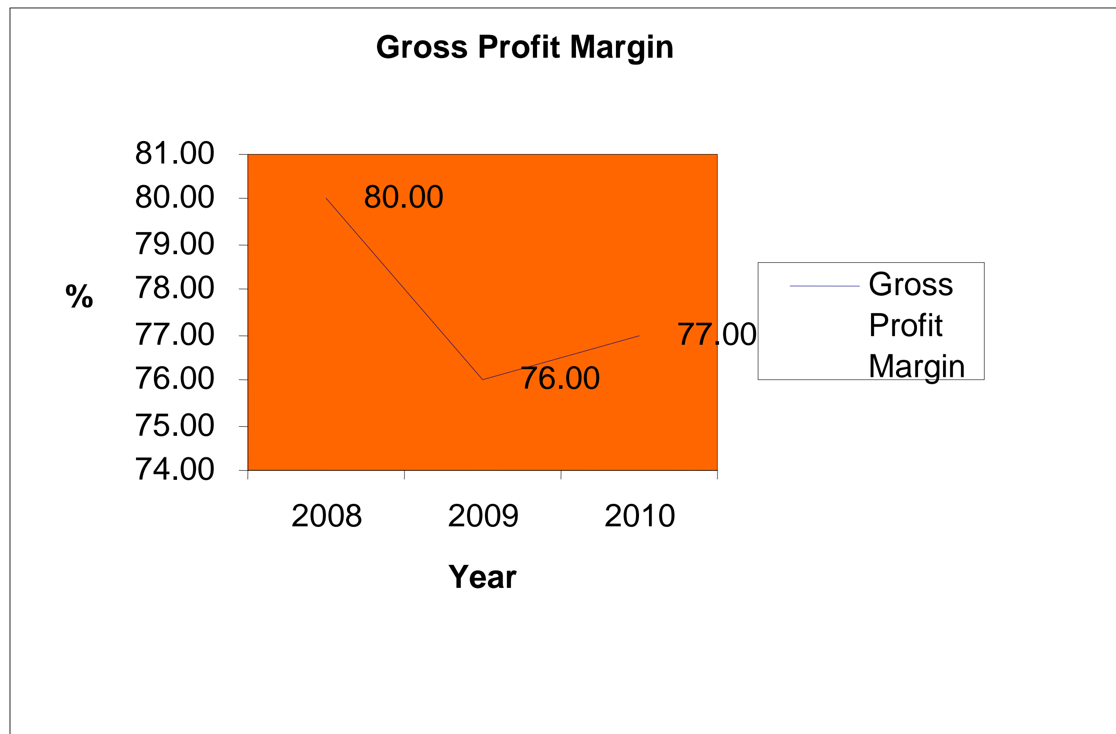

Figure 1: Gross Profit ratio of Breeze Beach Club

Source: Field work

ii) Net Profit Margin

The net profit margin is affected by more factors than the gross profit margin; that is obtained after deducting all expenses for particular year. The time –series analysis shown in figure 2 below indicates that for all years from 2008 to 2010 the hotel had not performed well; negative net profit margins of 6 percent, 24 percent, and 13 percent are observed in respective years. This means that the hotel has left nothing to benefit owners for the period of analysis (2008 to 2010). The main reason that contributes to the deterioration of net profit margin for the period under analysis was

caused by some costs which directly cannot be controlled by the management. The management has no control over the fixed charges such as, interest, tax and exchange rate fluctuation. When questioning the financial controller of the hotel, he indicated that the number of guests arrived in the hotel decreased in the year 2009 which was a factor that reduced net profit margin. The deterioration of net profit was also due to increase in the cost of running generator during the period of power blackout in 2010.

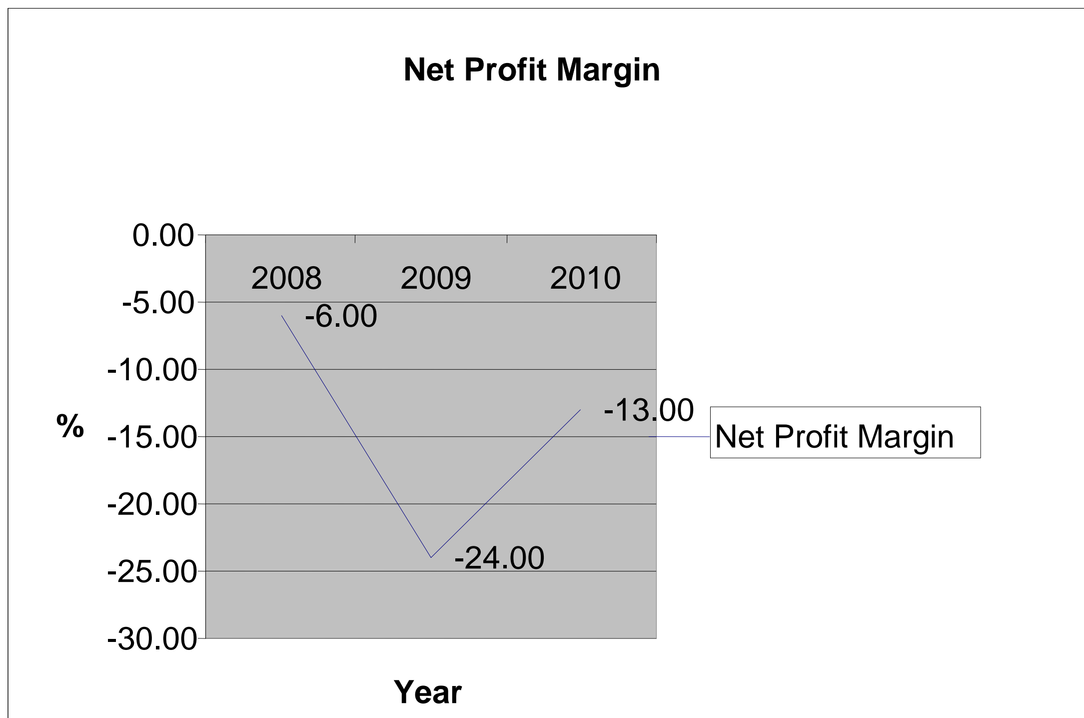

Figure 2: Net Profit ratio of Breeze Beach Club

Source: Field work

iii) Earnings Before Depreciation, Interest and Tax (EBDIT)

EBDIT is profit earned from business before consideration of depreciation, interest and tax. The trend shown in figure 3 below indicates that EBDIT Ratio for Breezes

Beach Club in year 2008 was 15 percent then plunged to 3 percent in the year 2009. In the year 2010, the ratio increased to 7 percent. This implies that 85 percent of revenue in the year 2008 has been consumed by the cost of goods sold and other operating expenses and left 15 percent of sales to cover for interest, depreciation, tax and earning to owners. In the year 2009, total operating cost was 97 percent of revenue and left only 3 percent to cover interest, depreciation, tax and earning to owners. The EBDIT Ratio also shows that 93 percent of revenue in the year 2010 was consumed by cost of goods sold and other operating costs and left only 7 percent to cover for depreciation, interest, tax and earning to owners.

The EBDIT Ratio and net profit ratio shown above clearly indicate that the hotel has not performed well during the period of analysis (2008 to 2010). The main reasons that contributed to lower returns in 2009 and 2010 were two major disasters that affected the whole hotel industry in Zanzibar. These were global financial crisis and power blackout. Both problems attributed to unfavourable returns to the hotel.

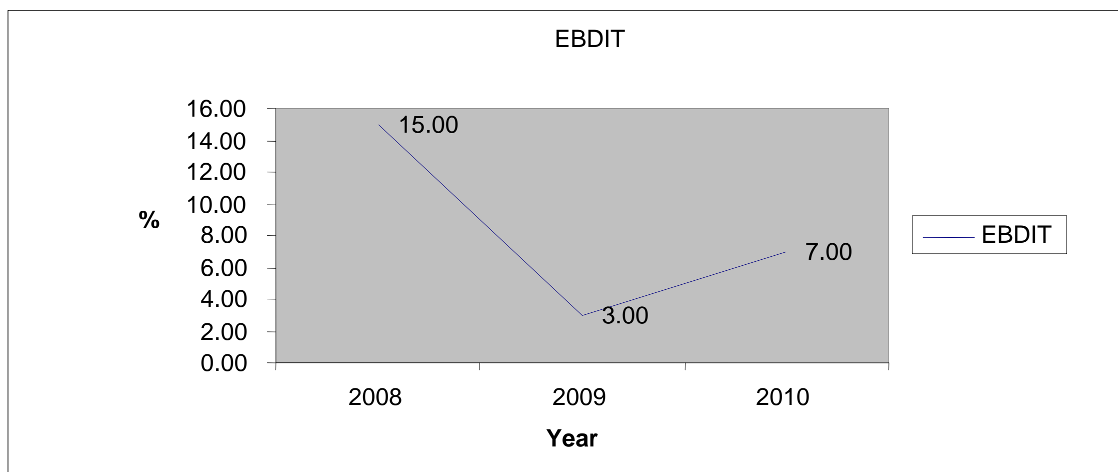

Figure 3: EBDIT ratio of Breeze Beach Club

Source: Field work

4.3.2 Liquidity Ratios

The liquidity ratio measures the ability of a business to meet its current and short term obligations. Liquidity ratios are numbers that provide an analysis of current assets against current liabilities. The difference between the two reflects the conversion and availability of liquid assets within the business. The liquidity ratios of Breeze Beach Club are shown below in table 8 below.

Table 8: Liquidity Ratios of Breezes Beach Club

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Liquidity	Current ratio	1.16	0.57	1.08
	Quick ratio	0.93	0.49	0.95
	Cash ratio	0.38	0.08	0.6

Source:Field work

i) Current Ratio

Current ratio measures the hotel's ability to meet its current obligations. Time-series analysis shown in figure 4 indicates that the current ratio of Breezes Beach Club is unstable. In the year 2008 as a base year the current ratio was 1.16 and then shrink to 0.57 in the year 2009, then in the year 2010 the current ratio increased to 1.08. The reason which attributes to shrink in current ratio in year 2009 is due to the increase in interest payable on the current liabilities.

As it can be seen on table 8, the current ratio of 1.16, 0.57 and 1.08 in the year 2008, 2009 and 2010 respectively mean that for every $1 of current liabilities, the hotel has current assets of $1.16, $0.57 and $1.08 in respective years. This means that in the year 2009 the hotel did not have enough current assets to meet its current obligations.

In other words, the hotel sometime uses the creditors' funds to finance its working capital. The current ratio represents a margin of safety for creditors. The higher the current ratio, the greater the margin of safety for suppliers. Figure 4 below show time-series analysis of current ratio for Breeze Beach Club.

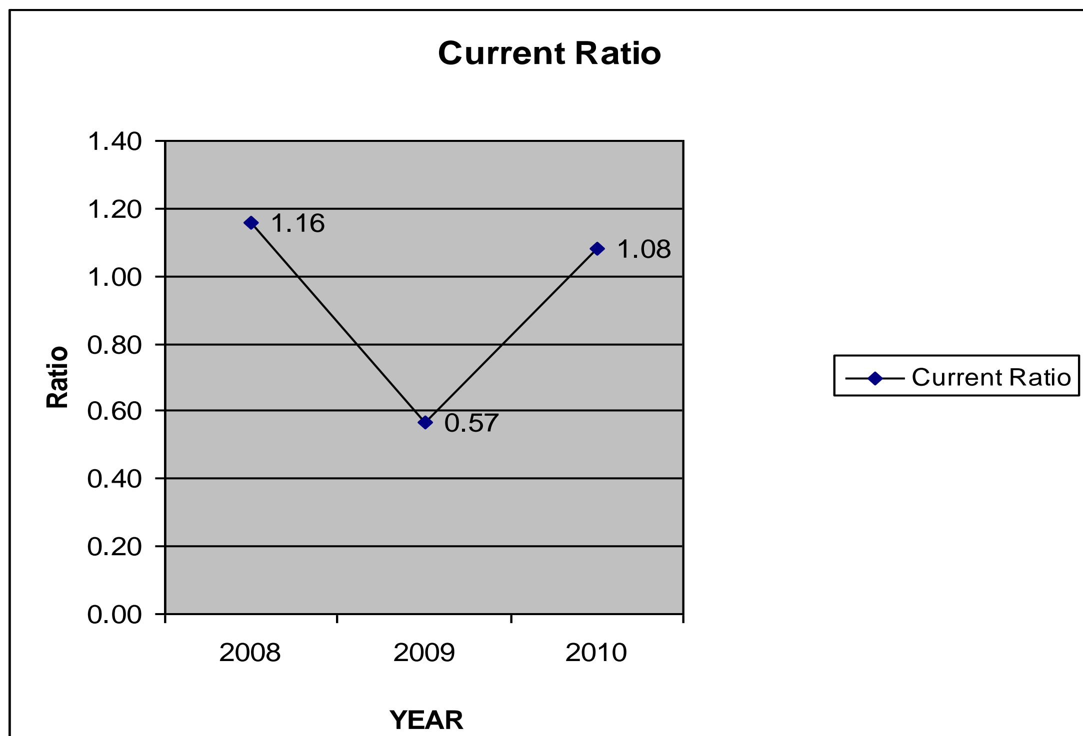

Figure 4: Current ratio of Breeze Beach Club

Source: Field work

ii) Quick Ratio

This ratio establishes a relationship between quick, or liquid, assets and current liabilities. An asset is liquid if it can be converted into cash immediately without loss of value. The quick ratio excludes inventory from current assets because it takes time in realizing cash. The Breezes Hotel's quick ratio plunged from 0.93 to 0.49 in the year 2009 and then increased to 0.95 in the year 2010(see figure 5 below). The

findings indicate that for every $1 of current liabilities, the hotel has $0.93, $0.49 and $0.95 in the year 2008, 2009, and 2010 respectively. Thus, if the hotel's inventories do not sell, and it has to pay all its current liabilities, it may find it difficult to meets its current obligations because its current assets are lower than current liabilities. This is to say that the hotel was in danger for all years from 2008 to 2010 and was unable to meet its current obligations. The hotel creditor's would be concerned with these low ratios and may demand cash payment or very short credit term. This situation may put the hotel at higher risk with creditors, and hence its operations do not portray a convincing business with profit.

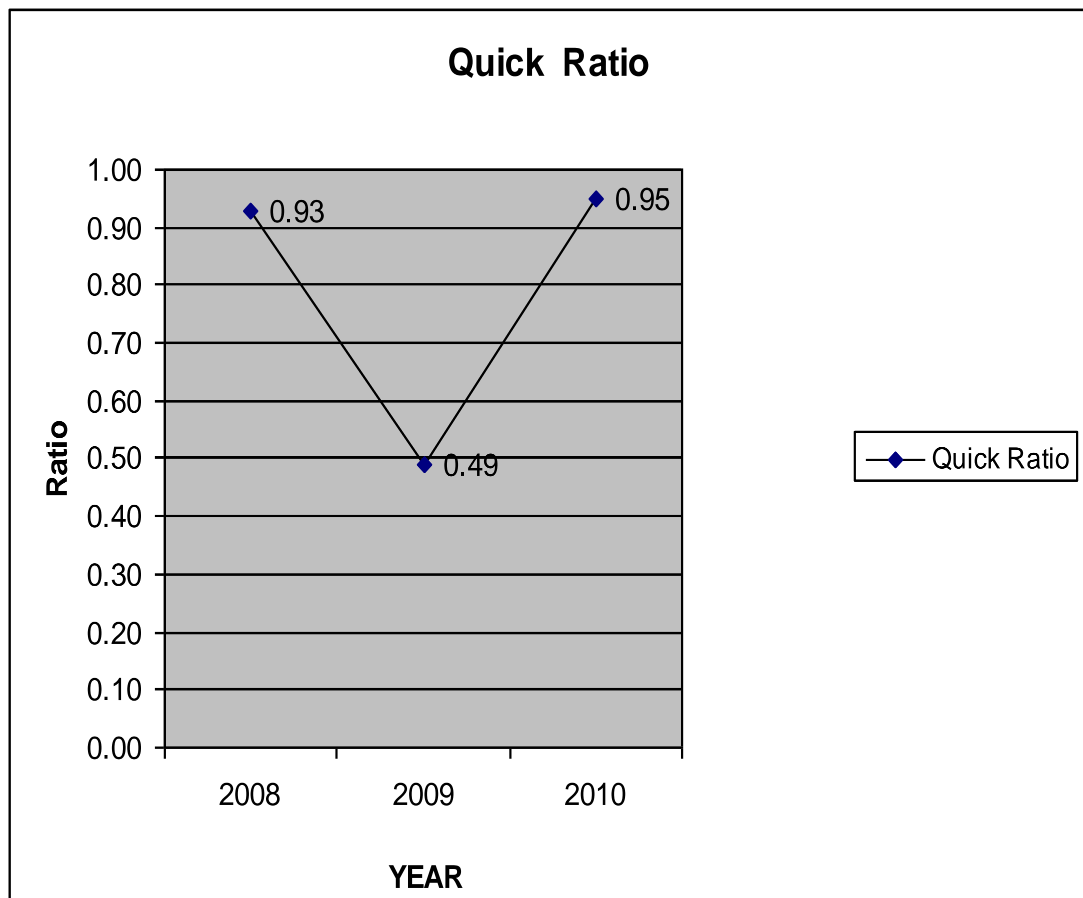

Figure 5: Quick Ratio Breeze Beach Club

Source: Field work

iii) Cash Ratio

Since cash is the most liquid assets, cash ratio examines the ratio of cash and its equivalent to current liabilities. The study observed that Breezes Hotel cash ratios decreased from 0.38 in the year 2008 to 0.08 in the year 2009 and then increase to 0.06 in the year 2010. This means that for every $1 of current liabilities the hotel carries $0.38, $0.08 and $0.6 for the year 2008, 2009, and 2010 respectively. The hotel carried small amount of cash to meet its creditors in case they demand immediate payments. Thus, the hotel was at higher risk of raising short term external funds (example bank loan) to meet current obligations. There is nothing to be worried if the hotel has reserve borrowing power. However, the hotel may lose opportunity to purchase supplies at cheap prices because cash purchase is normally cheaper than credit purchase. Figure 6 represents cash ratio time-series analysis for Breeze Beach Club.

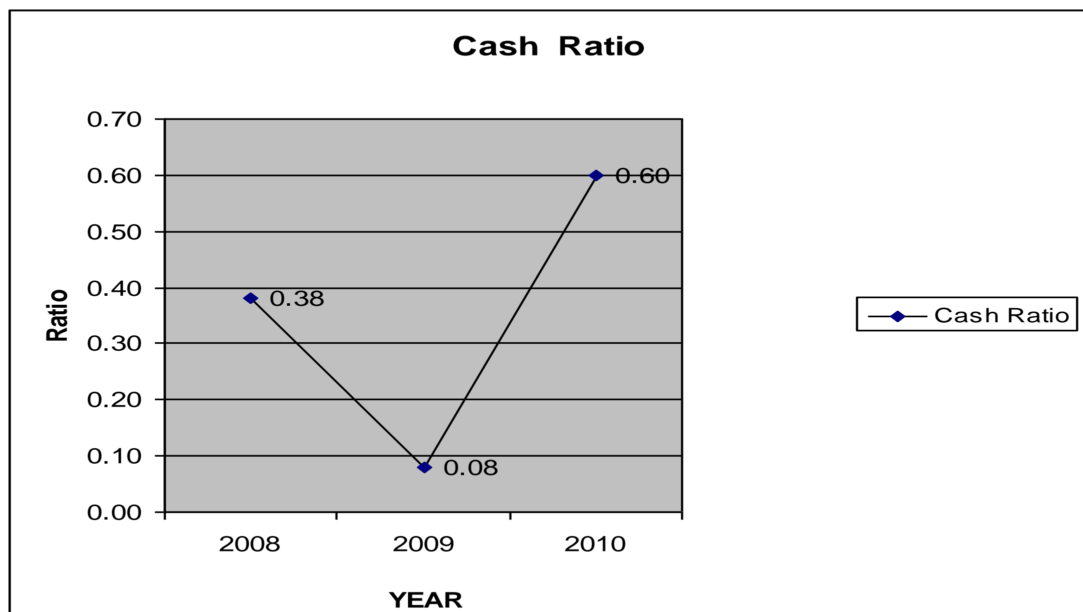

Figure 6: Cash Ratio of Breeze Beach Club

Source: Field work

4.3.3 Activity Ratios

Activity or efficiency ratios measure how well the company and its management use the assets under their control to generate sales and profits (Seng, 2001). Table 9 below represents activity ratios of Breeze Beach Club.

Table 9: Activity Ratios of Breezes Beach Club

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Activity	Inventory turnover	1.62	2.05	2.88
	Debtors turnover	14.74	10.60	18.29
	Total assets turnover	1.08	0.87	1.1

Source: Field work

i) Inventory Turnover

This ratio indicates the efficiency of the hotel in selling its product. The inventory turnover is shown in figure 7 below indicates that in 2008 Breeze Beach Club was turning its inventory of finished goods into sales (at cost) 1.62 times. In the year 2009 and 2010 inventory turnover increased to 2.05 and 2.88 times respectively. In other words, the hotel held average inventory of 12 months/1.62 = 7.4 months, 12 months/2.05 = 5.9 months, and 12 montsh/2.88 = 4.2 months in the year 2008, 2009, and 2010 respectively(see table 9). The average inventory of the hotel decreased year after year which implies that the hotel tried to minimize excessive inventory level. To hold excessive inventory level means that the hotel keep more inventory than demanded by production and sales activities. Therefore, the trend suggests that the Breeze Beach Club was in efficiently selling its products.

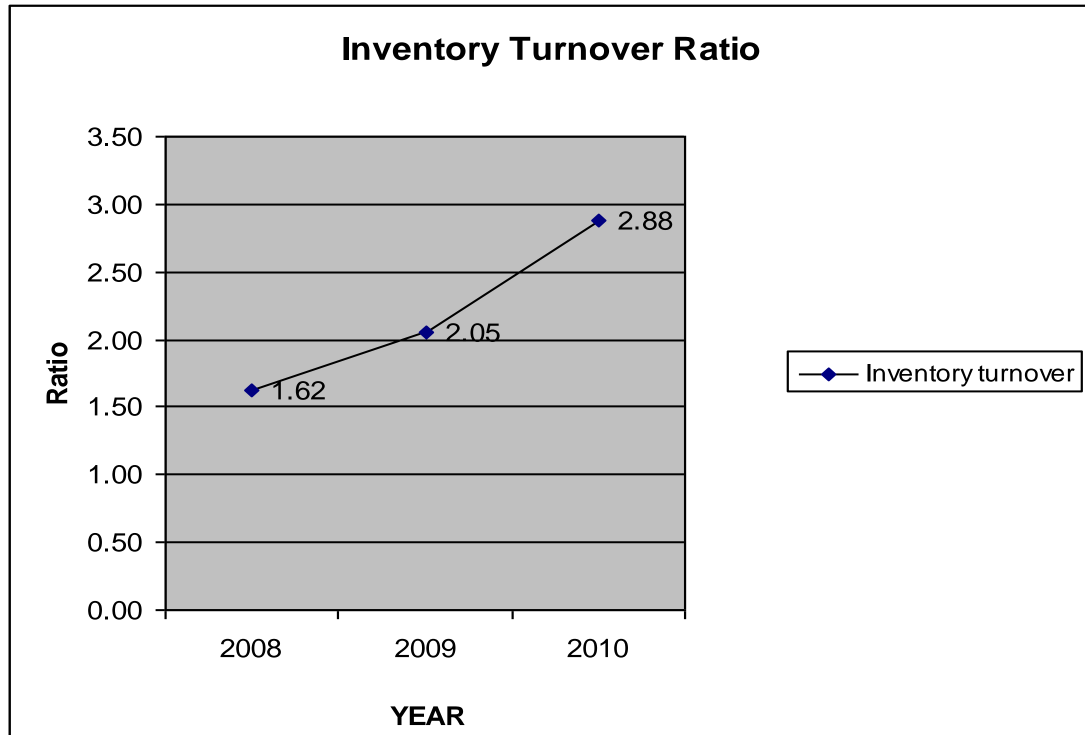

Figure 7: Inventory turnover of Breeze Beach Club

Source: Field work

ii) Debtor Turnover

Debtor turnover ratio assesses the speed of conversion from trade debtors into cash. Breeze Beach Hotel was able to convert (turnover) its debtors 14.74 times in year 2008. Then decreased to 10.6 times in year 2009 and then increased to 18.29 times in the year 2010. In other words, the hotel book debts (account receivables) remain outstanding for 12 months/14.74 = 0.8 month in year 2008, 12 months/10.6 = 1.1 month in year 2009 and 12 months/18.29 = 0.66 month in year 2010. This implies that the hotel was efficient in turning its debtors into cash and therefore the chance of bad debts is narrow. Figure 8 below represents time-series analysis of debtors turnover ratio for Breeze Beach Hotel.

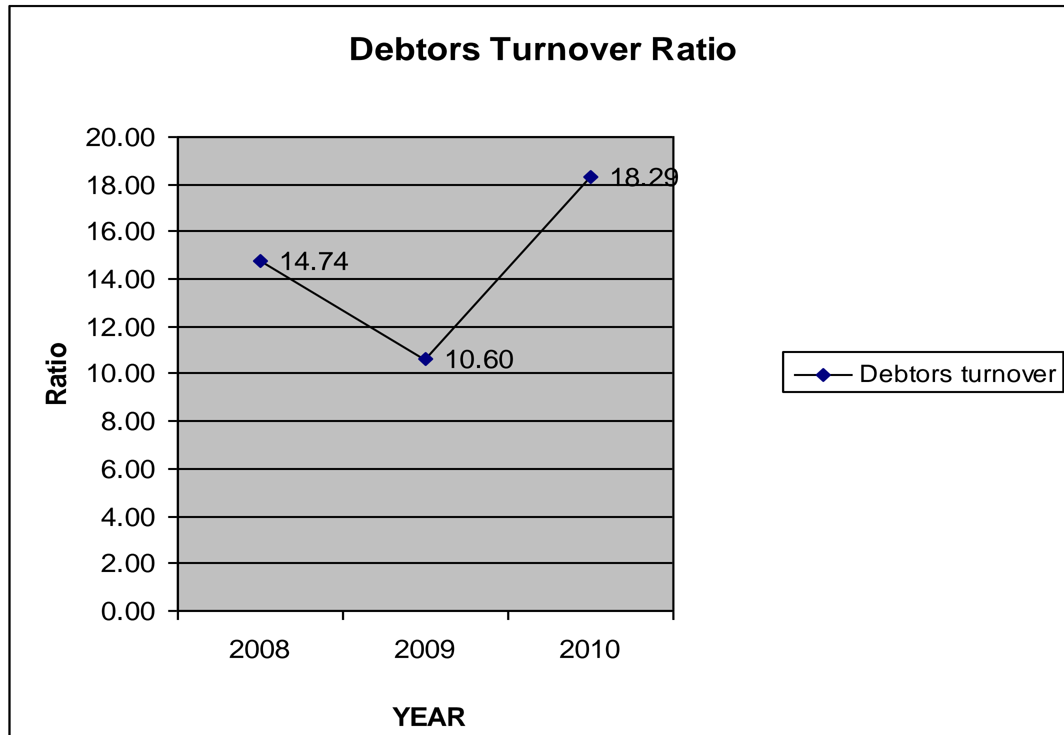

Figure 8: Debtors turnover of Breeze Beach Club

Source: Field work

iii) Total Assets Turnover

This ratio shows the firm's ability in generating sales from all financial resources committed to total assets. The findings represented in figure 9 below show that total assets turnover was 1.08 times in 2008, then decreased to 0.87 times in year 2009 and increased to 1.1 times in year 2010. This implies that in year 2010 the hotel generated a sale of USD 1.1 for every dollar of investment in fixed assets and current assets together, which is higher compared to 2008 and 2009 where the hotel generated a sale of USD 1.08 and USD 0.87 respectively. Creditors, owners, and managers like to see this ratio as high as possible because it measures how effectively total assets are used to generate revenue.

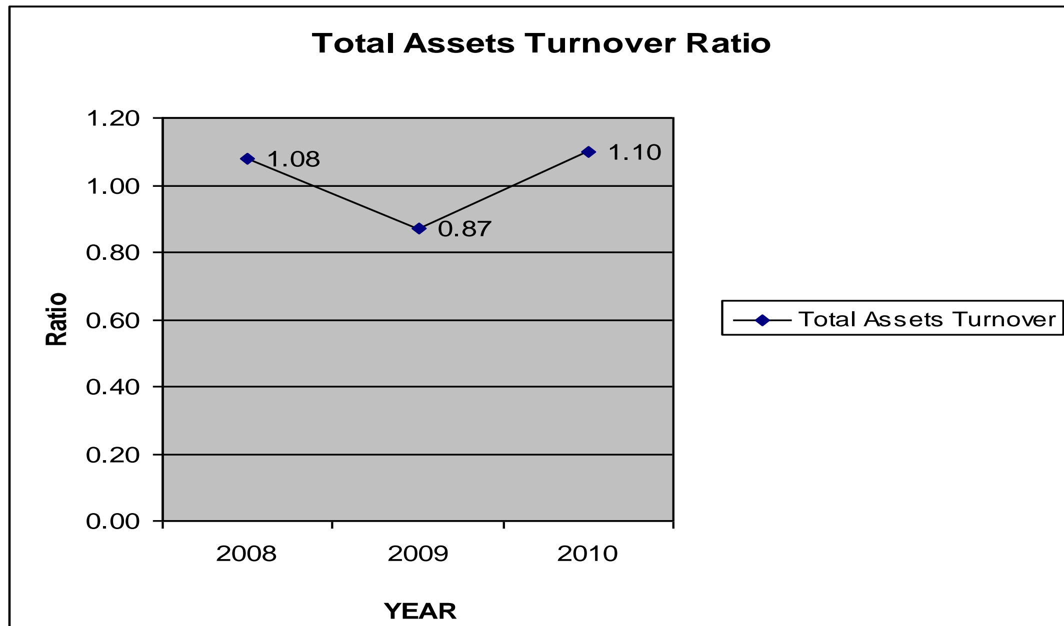

Figure 9: Total assets turnover of Breeze Beach Club

Source: Field work

4.3.4 Leverage Ratio

Leverage ratios show the extent to which debt is used in a company's capital structure. Table 10 represents leverage ratios of Breeze Beach Club.

Table 10. Leverage Ratios of Breeze Beach Club

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Leverage	Total debt	1.06	1.28	1.41
	Debt-equity ratio	(16.60)	(4.53)	(3.46)

Source:Field work

i) Total Debt Ratio

This is a ratio indicating the proportion of debt a hotel has relative to its assets; it gives a general idea of the leverage of the company along with the potential risks the

company faces in terms of its debt load. The ratio indicates what proportion of a company’s financing asset is from debt, making it a good way to check a company’s long-term solvency. In general, a lower ratio is better. Value of 1 or less in debt ratios shows good financial health of a company. Used in conjunction with other measures of financial health, the debt ratio helps investors to determine a company's level of risk.

The Breeze Beach Club has debt ratio of 1.06 in year 2008, then increased to 1.28 in year 2009. The ratio continued to increase up to 1.41 in year 2010. This means that for every dollar of assets the hotel has debt of USD 1.06, USD 1.28, and USD 1.41 for the year 2008, 2009, and 2010 respectively. This implies that the hotel heavily relies on debt to finance its assets which is more risky for the business. Figure 10 shows time-series analysis for debt ratio of Breeze Beach Club.

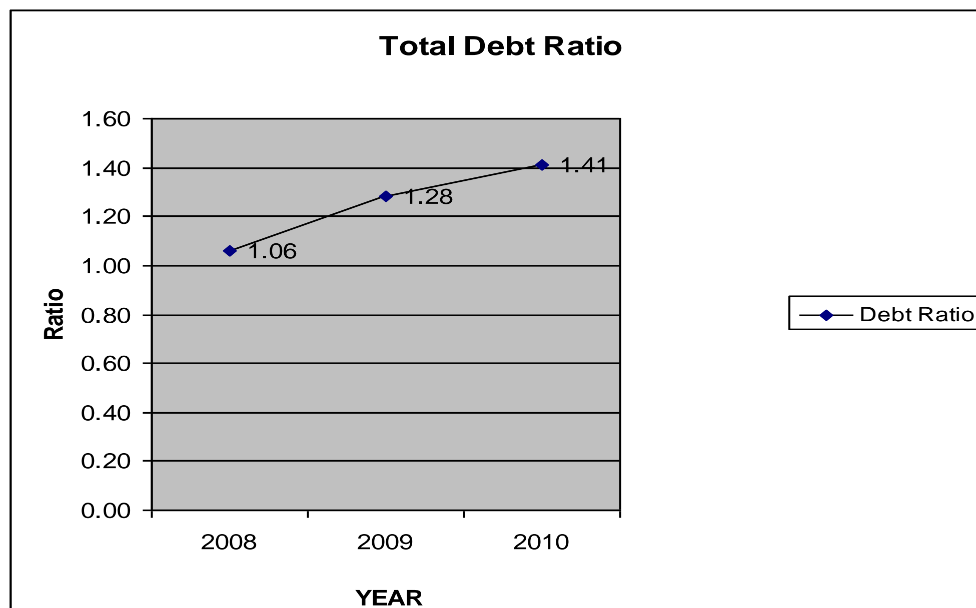

Figure 10: Debt Ratio of Breeze Beach Club

Source: Field work

ii) Debt-equity Ratio

Debt-to-equity Ratio indicates the relationship between the external equities or outsiders' funds and the internal equities or shareholders' funds. It is also known as external-internal equity ratio. It is determined to ascertain soundness of the long term financial policies of the company. Figure 11 below shows debt-equity ratio of Breeze Beach Hotel which indicates that in year 2008 outsiders contributed USD 16.6 for every dollar of internal equities. In year 2009 outsiders contributed USD 4.53 for every dollar of internal equities. The lenders contributions from outsiders decreased to USD 3.46 for every dollar of internal equities in year 2010. It should be noted that negative debt-equity ratio means that the owners have lesser equity caused by previous huge losses. In case liquidation happens immediately the owners will have nothing to claim.

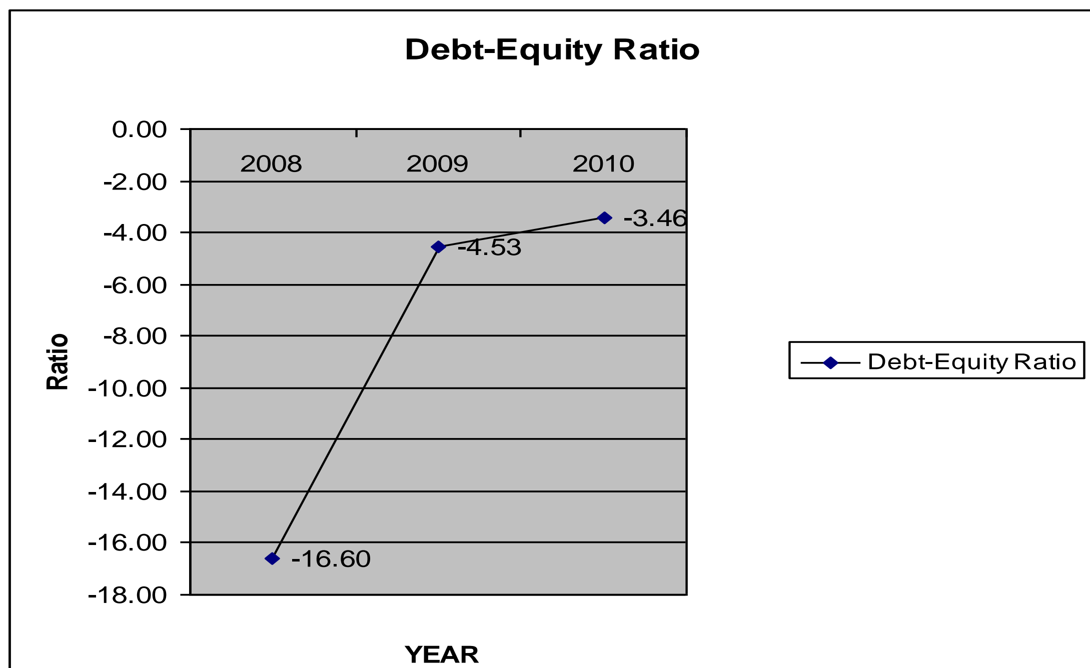

Figure 11: Debt – equity Ratio of Breeze Beach Club

Source: Field work

4.4.0 Time Analysis of Veraclub Zanzibar

4.4.1 Profitability Ratios

Profitability ratios replicate the results of all areas of management's responsibilities (Schmidgall, 2006). Table 11 below represents profitability ratios for Veraclub Zanzibar Ltd.

Table 11: Profitability Ratios of Vera Club Zanzibar

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Profitability	Gross Profit Margin	70 percent	71 percent	72 percent
	Net Profit Margin	0.3 percent	1 percent	-1 percent
	EBDIT	2 percent	3 percent	3 percent

Source:Field work

i) Gross Profit Margin

The gross profit margin shows profit relative to sales after the deduction of production cost, and indicates the relation between production costs and selling price. The pattern in figure 12 below shows that the gross profit margin of Vera Club improved year after year even though in small percentage. In the year 2010 the gross profit margin was 72 percent, which is better compared to 71 percent and 70 percent in the year 2009 and 2008 respectively. The ratios imply that the hotel left between 70 percent and 72 percent to cover for other operating expensive and benefits to the owners. Despite financial crisis of 2009 and 2010 that affected tourism industry, the management of Vera Club was able to control the production cost to keep it at

minimum which caused the gross profit margin to improve. Other reason that caused gross profit margin to improve was a change in room rate per pax from USD 46 in the year 2008 to USD 50 in the year 2009 and USD 55 in the year 2010.

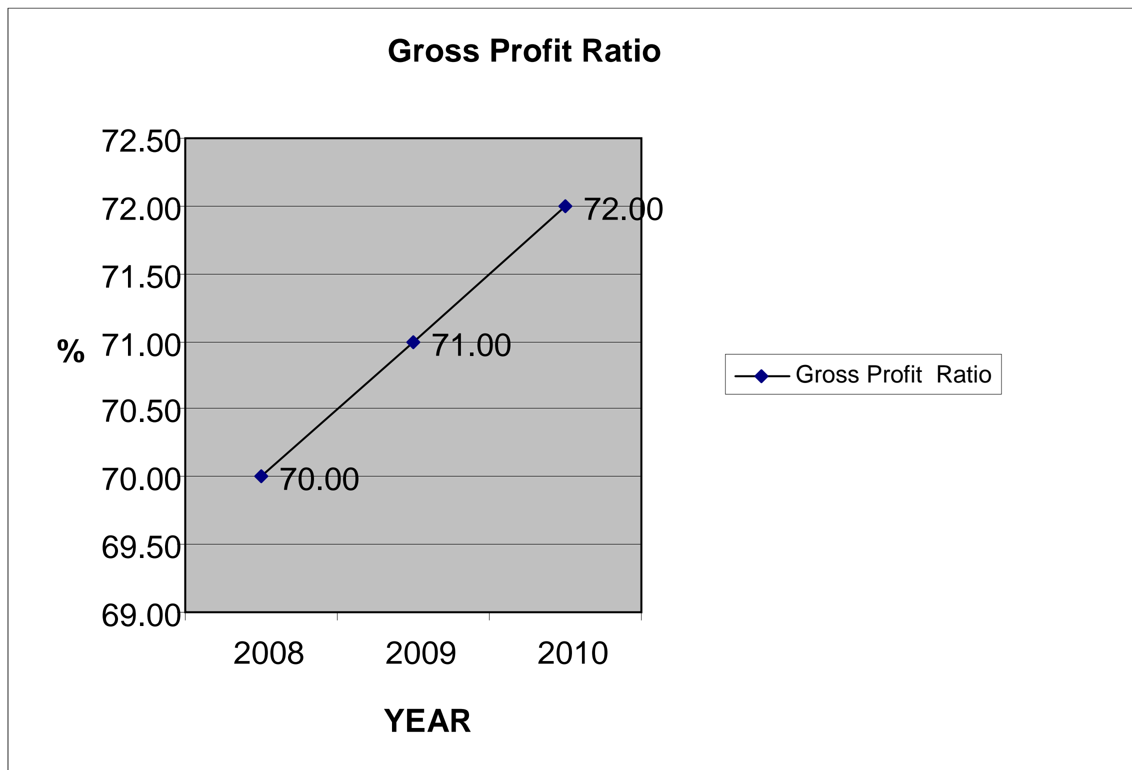

Figure 12: Gross Profit Margin Ratio of Veraclub Zanzibar Ltd

Source: Field work

ii) Net Profit Margin

The net profit margin is affected by more factors than the gross profit margin; that is obtained after deducting all expenses for particular year. The results shown in figure 13 below indicate that in the year 2009 the hotel performed better by obtaining net profit margin of 1 percent compared to net profit margin of 0.3 percent and negative 1 in the year 2008 and 2009 respectively. In the year 2010 Veraclub leased additional hotel at Nungwi Zanzibar. This caused increased running cost such as lease rent,

repair and maintenance and salary and wages. The costs also increased due to increase cost of running generators during period of power blackout in Zanzibar.

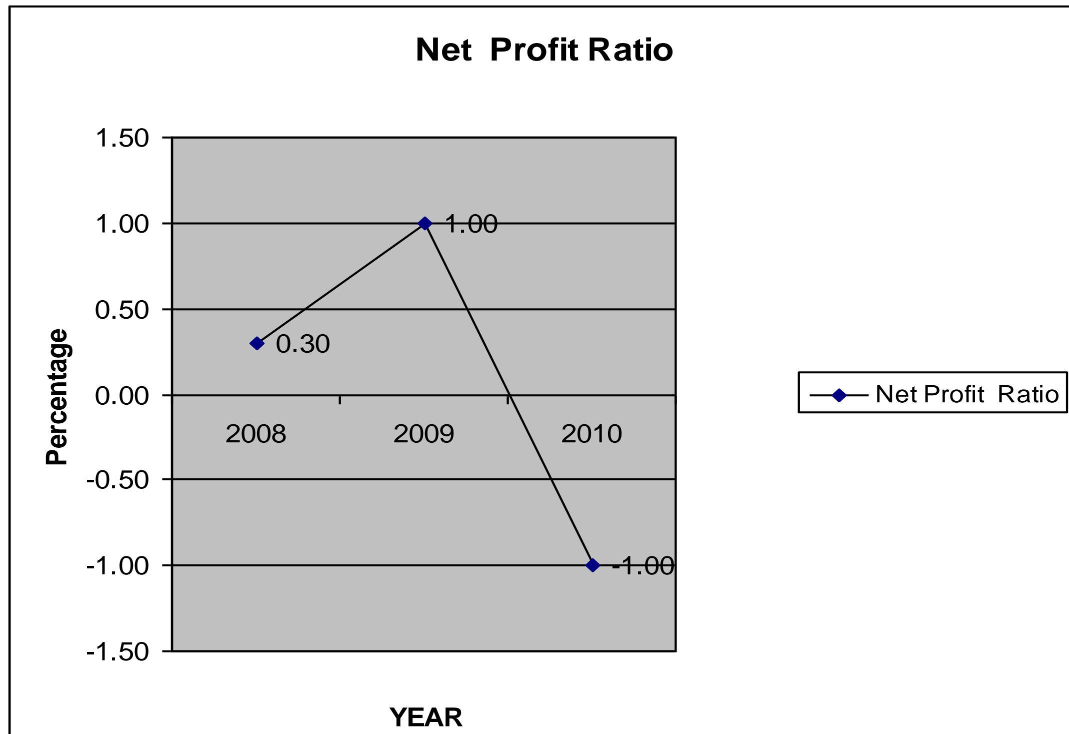

Figure 13: Net Profit Margin Ratio of Veraclub Zanzibar Ltd

Source: Field work

iii) Earning Before Depreciation, Interest and Tax (EBDIT)

EBDIT is a profit earned from business before consideration of depreciation, interest and tax. The EBDIT Ratio for Veraclub Zanzibar Ltd as shown in figure 14 below indicates that in year 2008 the ratio was 2 percent then increased to 3 percent in the year 2009. In the year 2010, the ratio was the same as in the year 2009. This means that 98 percent of revenue in the year 2008 has been consumed by the cost of goods sold and other operating expenses and left only 2 percent of sales to cover for depreciation, tax and earning to owners. In the year 2009 and 2010, only 3 percent

was left to cover depreciation, tax and earning to owner. This implies that between 2009 and 2010 there was no significant change between revenue and operating cost which is good indication for survival of the business.

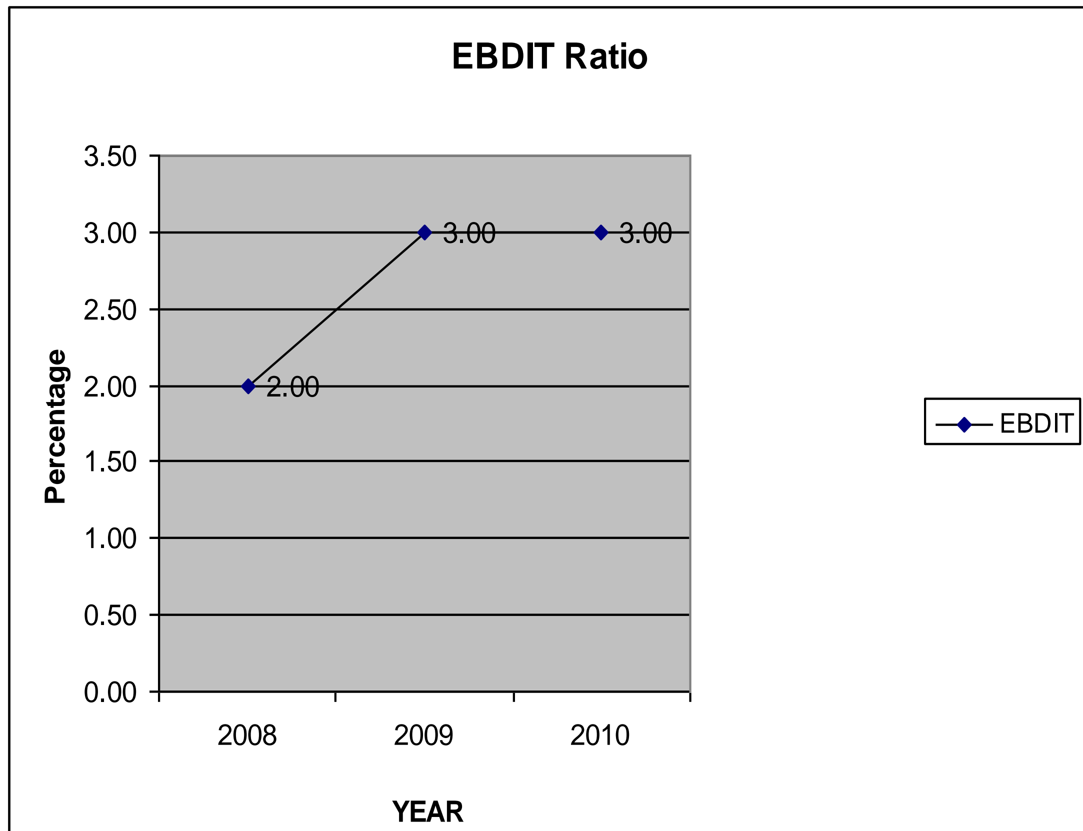

Figure 14: EBDIT Ratio of Veraclub Zanzibar Ltd

Source: Field work

4.4.2 Liquidity Ratio

The liquidity ratio measures the ability of a business to meet its current and short term obligations. Liquidity ratios are numbers that provide an analysis of current assets against current liabilities. The difference between the two reflects the conversion and availability of liquid assets within the business. The liquidity ratios of Breeze Beach Club are shown below in table 12.

Table 12: Liquidity Ratios of Vera Club Zanzibar

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Liquidity	Current ratio	1.09	1.15	1.0
	Quick ratio	0.95	0.99	0.94
	Cash ratio	0.17	0.06	0.05

Source:Field work

i) Current Ratio

Liquidity ratio measures the hotel's ability to meet its current obligations. Figure 15 below shows that current ratio of Vera Club Zanzibar is fluctuating within acceptable range. In year 2008 as a base year the current ratio was 1.09, then increase to 1.15 in year 2009, and then decrease to 1.0 in year 2010. The main reason for decrease in current ratio in year 2010 was due to increase in current liabilities after the hotel obtained fund from tour operator who also is shareholder of the hotel to finance lease of new hotel.

The current ratio of 1.09, 1.15 and 1.0 in the year 2008, 2009 and 2010 respectively mean that for every $1 of current liabilities, the hotel has $1.09, $1.15 and $1.0 in respective years. This means that the hotel has enough current assets to meet its current obligations. In other words, the hotel uses or depend much on its own resources to finance its working capital. Therefore, the suppliers are safer to do the business with the hotel.

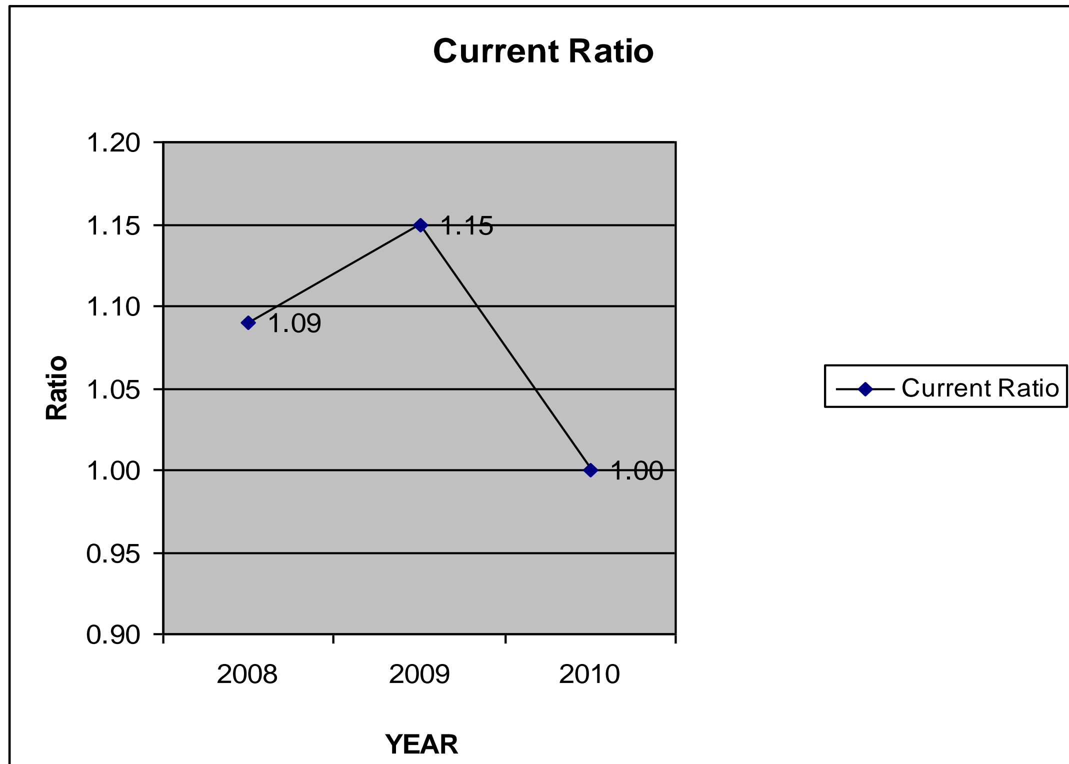

Figure 15: Current Ratio of Veraclub Zanzibar Ltd

Source: Field work

ii) Quick Ratio

This ratio establishes a relationship between quick, or liquid, assets and current liabilities. An asset is liquid if it can be converted into cash immediately without loss of value. The quick ratio excludes inventory from current assets because it takes time for realizing into cash. The Vera Club Hotel's quick ratio increased from 0.95 in year 2008 to 0.99 in year 2009 and then decreased to 0.94 in the year 2010(see time-series analysis in figure 16 below). The result indicates that for every $1 of current liabilities, the hotel has $0.95, $0.99 and $0.94 in the year 2008, 2009, and 2010 respectively. Thus, if the hotel's inventories do not sell, and it has to pay all its current liabilities, it may find it little difficult to meet its current obligations because

its current assets are lower than current liabilities. In the suppliers' perspective, the hotel was in a little danger for all years from 2008 to 2010 to meet their current obligations. The hotel creditor's would be concerned with these low ratios and may demand cash payment or very short credit term. This situation may put the hotel at higher risk with creditors.

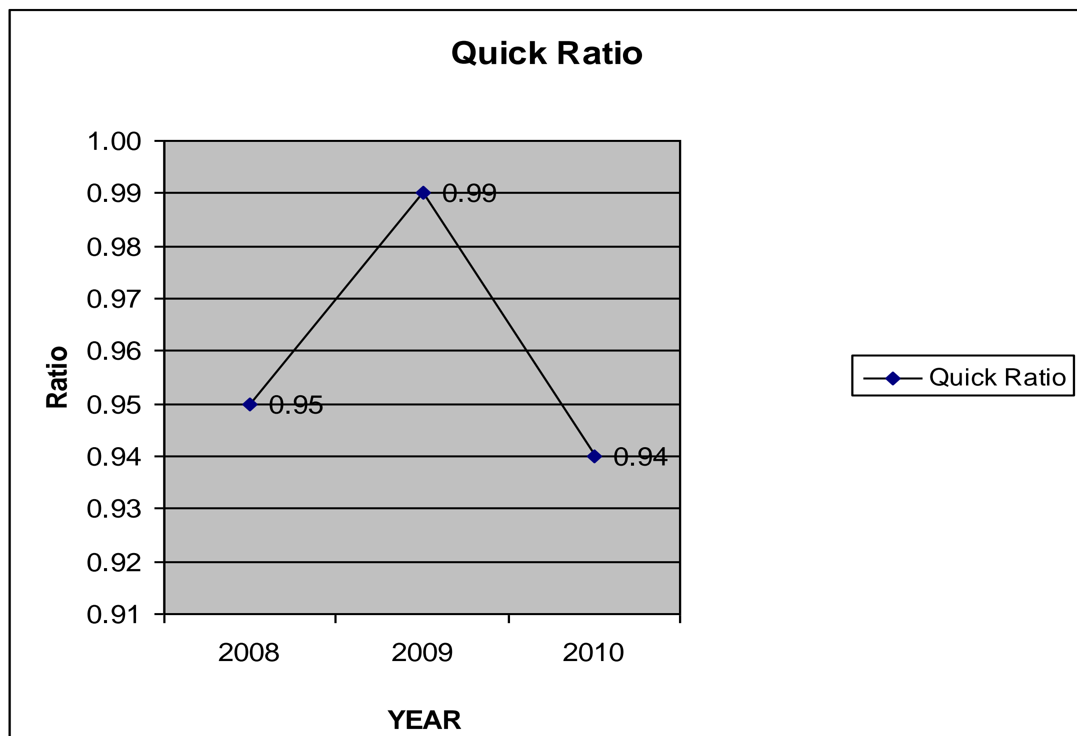

Figure 16: Quick Ratio of Veraclub Zanzibar Ltd

Source: Field work

iii) Cash Ratio

Since cash is the most liquid assets, cash ratio examines the ratio of cash and its equivalent to current liabilities. The Vera Club Hotel cash ratios as it appeared in figure 17 below decreased from 0.17 in the year 2008 to 0.06 in the year 2009 and then continue to decrease to 0.05 in the year 2010. This means that for every $1 of current liabilities the hotel carries cash of $0.17, $0.06 and $0.05 for the year 2008,

2009, and 2010 respectively. The hotel carried small amount of cash to meet its creditors in case they demand immediate payments. Thus, the hotel was at higher risk of cost of raising short term fund externally (example bank loan) to meet current obligations. However, the company may use the relationship with its trade debtor (sole tour operator of the hotel) to raise cash when needed.

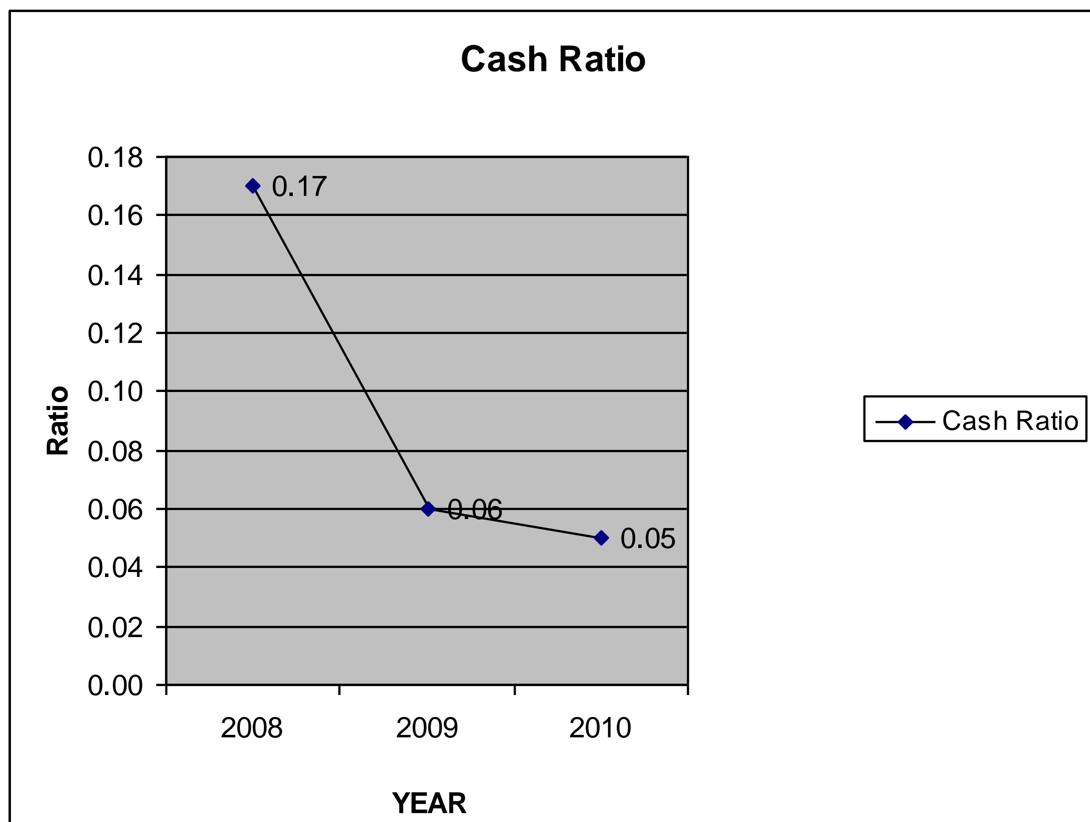

Figure 17: Cash Ratio of Veraclub Zanzibar Ltd

Source: Field work

4.4.3 Activity Ratio

Activity or efficiency ratios measures how well the company and its management use the assets under their control to generate sales and profits (Seng, 2001). Table 13 below represents Activity Ratios of Veraclub Zanzibar Ltd.

Table 13: Activity Ratios of Veraclub Zanzibar Ltd

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Activity	Inventory turnover	2.9	3.02	2.85
	Debtors turnover	8.06	9.30	3.02
	Total assets turnover	4.19	4.87	1.99

Source:Field work

i) Inventory Turnover

This ratio indicates the efficiency of the hotel in selling its product. The results of inventory turnover as shown in figure 18 below show that in 2008 Veraclub was turning its inventory of finished goods into sales (at cost) 2.9 times. In the year 2009 inventory turnover increased to 3.02 times then decreased to 2.85 times in the year 2010. In other words, the hotel hold average inventory of 12 months/2.9 = 4.1 months, 12 months/3.02 = 4 months, and 12 montsh/2.85 = 4.2 months in the year 2008, 2009, and 2010 respectively. The average inventory of the hotel was not uniform (that is it slight varies year after year) which suggest that the hotel sometimes hold excessive inventory level and other time hold low level of inventory. The excessive inventory level means that the hotel keeps more inventory than demanded by production and sales activities and low level means that the hotel run in stock outs (that living from hand to mouth).

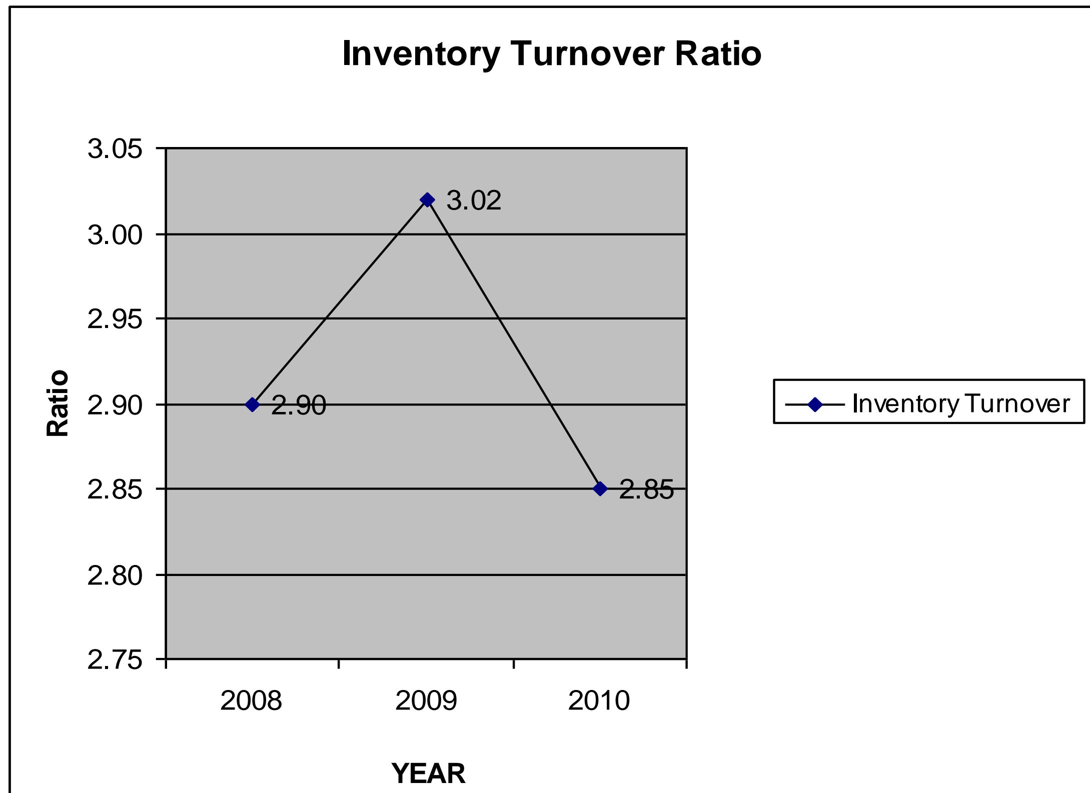

Figure 18: Inventory turnover of Veraclub Zanzibar Ltd

Source: Field work

ii) Debtor Turnover

Debtor turnover ratio assesses the speed of conversion from trade debtors into cash. Veraclub Hotel was able to turnover its debtors 8.06 times in year 2008. Then increased to 9.3 times in year 2009 and thereafter decreased to 3.02 times in the year 2010. In other words, the hotel book debts (account receivables) remain outstanding for 12 months/8.06 = 1.49 month in year 2008, 12 months/9.30 = 1.29 month in year 2009 and 12 months/3.02 = 3.97 month in year 2010. The results show that in 2009 the hotel had collect its receivable little faster compared to the year 2008 and 2010. Figure 19 below shows debtor turnover ratio of Veraclub Zanzibar Ltd.

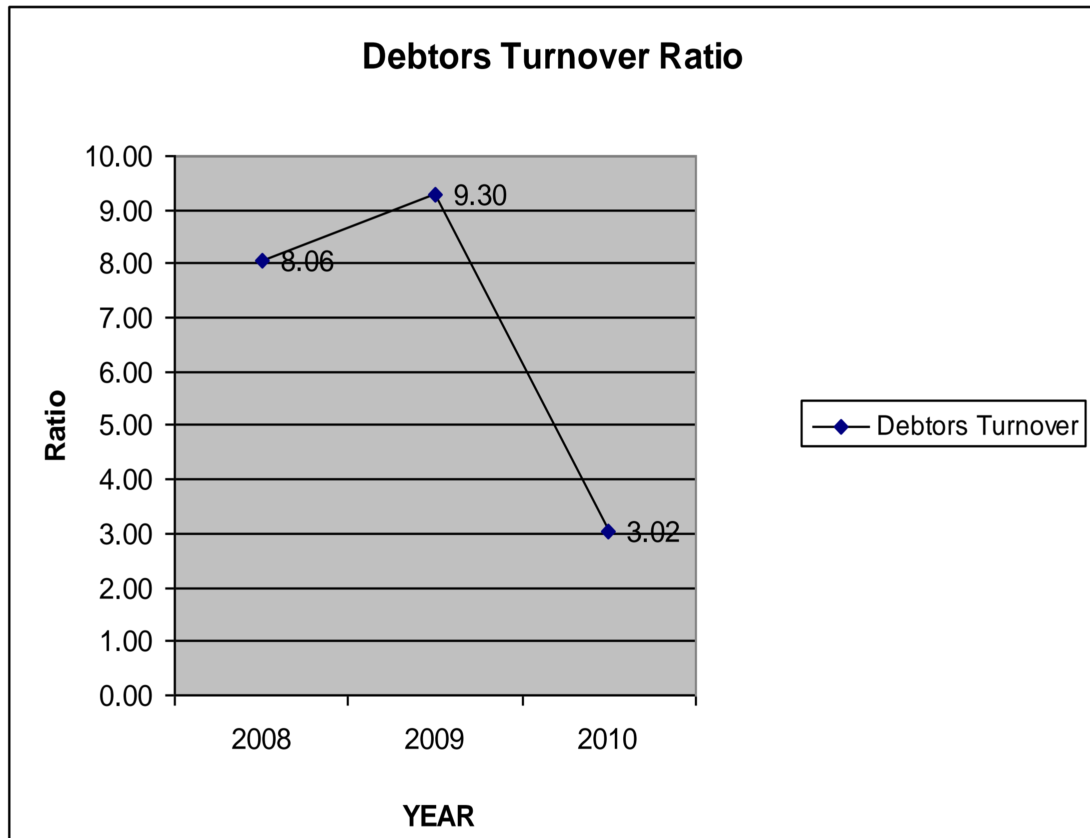

Figure 19: Debtors turnover of Veraclub Zanzibar Ltd

Source: Field work

iii) Total Assets Turnover

This ratio shows the firm's ability in generating sales from all financial resources committed to total assets. The trend analysis shown in figure 20 below indicates that total assets turnover was 4.19 times in 2008, then increased to 4.87 times in year 2009 and thereafter decreased to 1.99 times in year 2010. This means that in 2009 the hotel generated a sale of USD 4.87 for every dollar investment in fixed assets and current assets together, which was higher compared to 2008 and 2009 where the hotel generated a sale of USD 4.19 and USD 1.99 respectively.

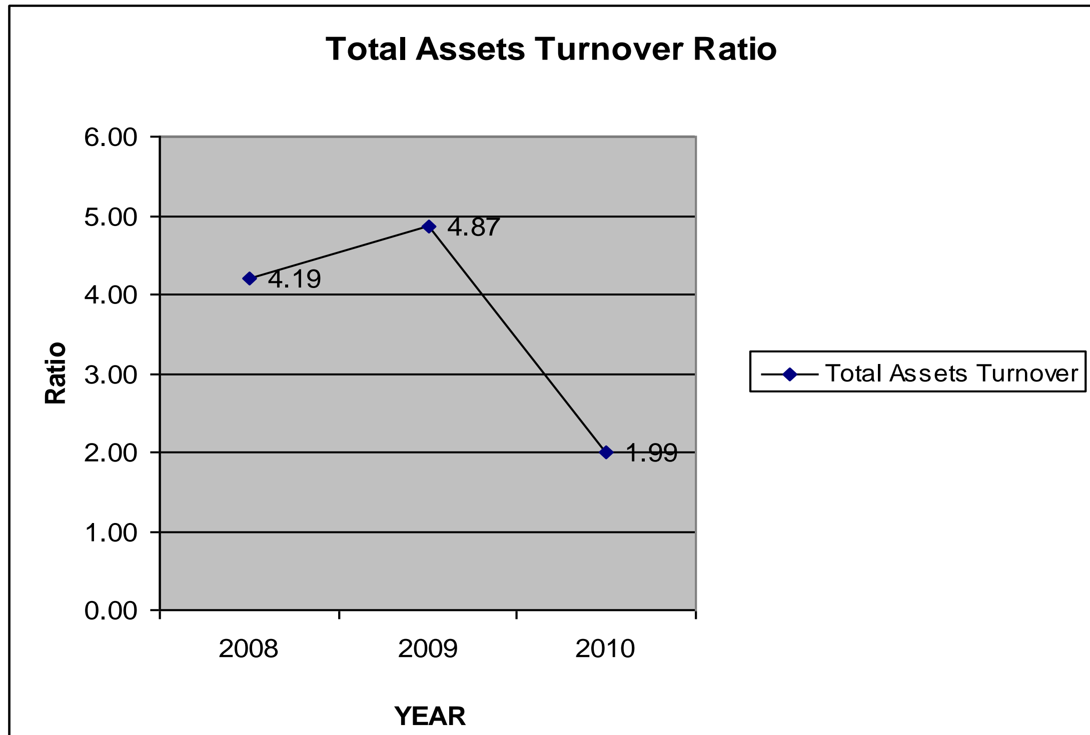

Figure 20: Total assets turnover of Veraclub Zanzibar Ltd

Source: Field work

4.4.4 Leverage Ratio

Leverage Ratios show the extent to which debt is used in a company's capital structure. Table 14 represents leverage ratios of Veraclub Zanzibar Ltd.

Table 14: Leverage Ratios of Veraclub Zanzibar

Ratio Category	Ratio	Year 2008	Year 2009	Year 2010
Leverage	Debt ratio	0.75	0.67	0.89
	Debt-equity ratio	3.05	2.06	7.83

Source:Field work

i) Debt Ratio

Debt Ratio will tell how much the hotel relies on debt to finance its assets. The ratio may be used to analyse the long-term solvency of a firm. The findings of this study show that debt ratio of Veraclub Zanzibar fluctuated whereby it was 0.75 in year 2008, then decreased to 0.67 in year 2009 and thereafter increased to 0.89 in year 2010. This means that for every dollar of assets the hotel has debt of USD 0.75, USD 0.67 and USD 0.89 for the year 2008, 2009, and 2010 respectively. This implies that the hotel was relying on debt to finance its assets which is less risky by the hotel. Figure 21 below represents time-series analysis of debt ratio of Veraclub Zanzibar Ltd.

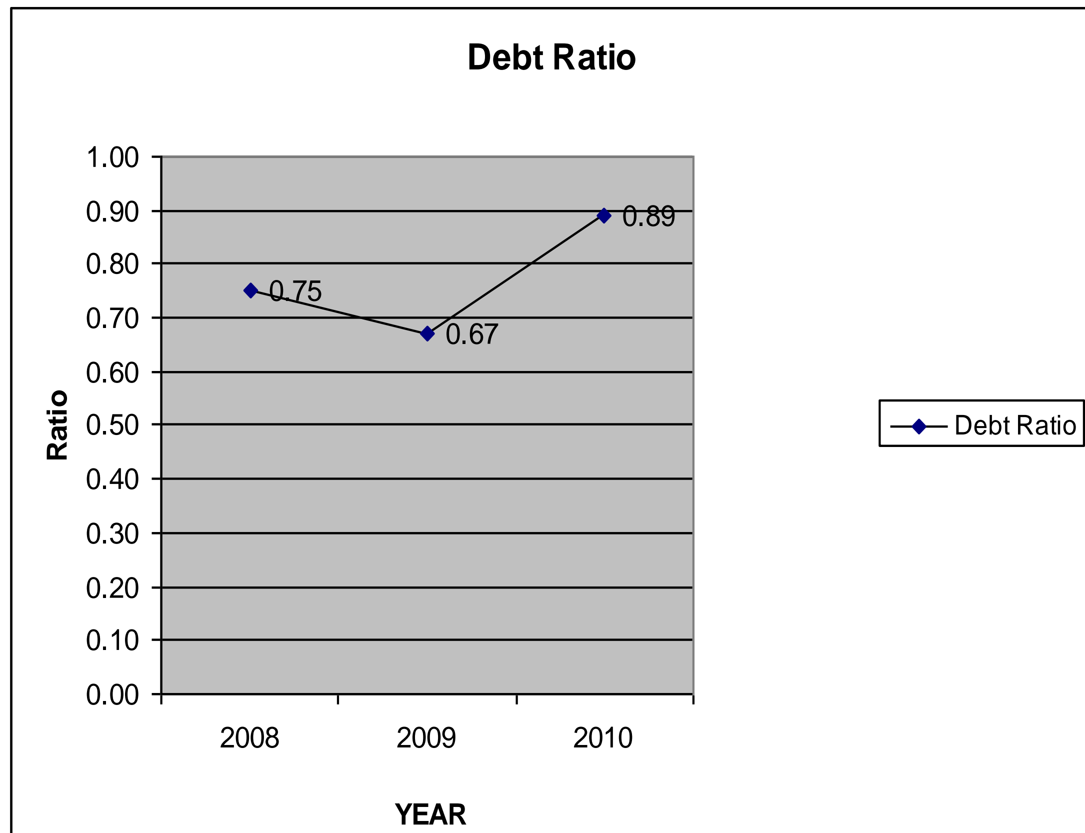

Figure 21: Debt ratio of Veraclub Zanzibar Ltd

Source: Field work

ii) Debt-equity Ratio

This ratio describes the lenders' contribution for each dollar of the owners' contribution. In case of Veraclub Zanzibar, the ratio shows that outsiders contribute USD 3.05, USD 2.06 and USD 7.83 for every dollar of internal equities for the year 2008, 2009, and 2010 respectively. Figure 22 below indicates that in 2010 the ratios increased from 2.06 to 7.83. The reason behind this was due to increase in liabilities for raising fund to finance lease of additional hotel (Sunset Hotel). The result is that for every dollar invested by shareholders, creditors topped up USD 7.83. That is to say external funding is higher than internal sources which is more risky for the hotel.

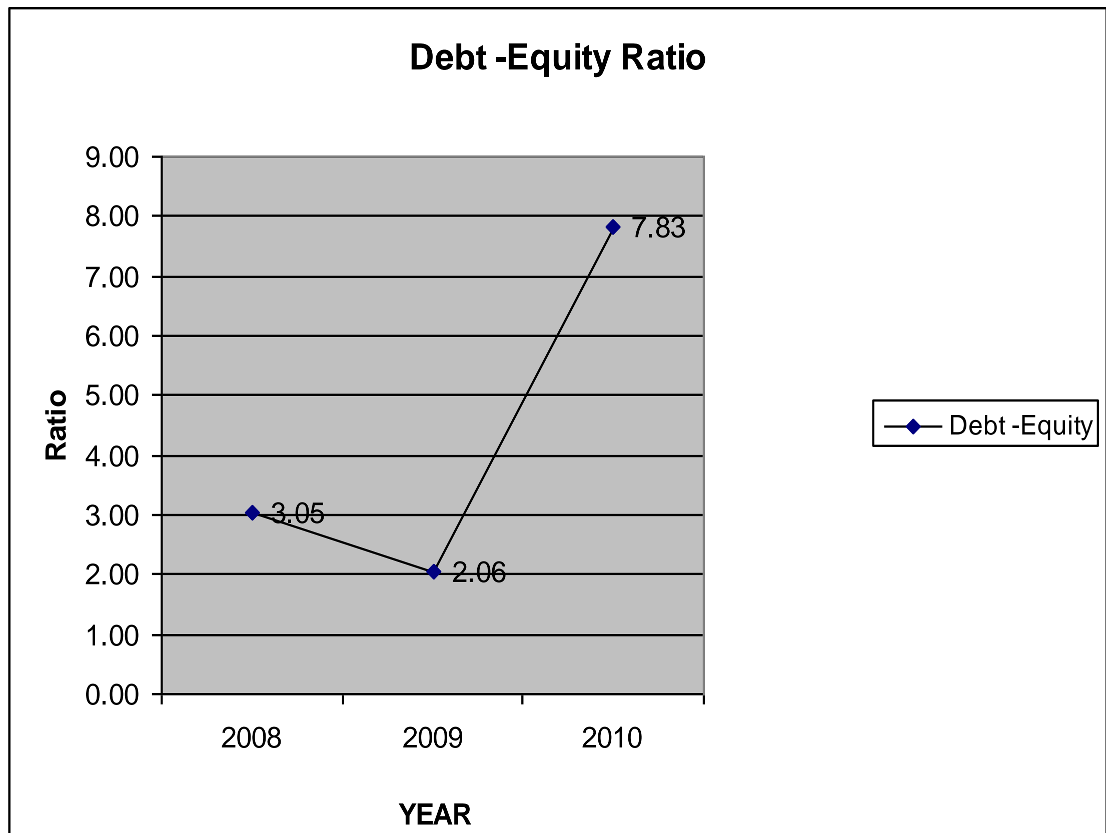

Figure 22: Debt –equity ratio of Veraclub Zanzibar Ltd

Source: Field work

4.5.0 Cross-Sectional Analysis

The financial ratios of Package hotel (Veraclub) have been compared to Non Package hotel (Breeze Beach Club) in order to determine their financial conditions and performance. The research findings are explained here under:-

4.5.1 Profitability Ratio

Profitability ratio measure the results of business operations or overall performance and effectiveness of the hotels. The primary objective of a business undertaking is to earn profits. Profit is the engine that drives the business enterprise. A business needs profits not only for its existence but also for its expansion and diversification. Table 15 below represents profitability ratios for two hotels.

Table 15: Profitability ratios between Breeze Beach Club and Veraclub Zanzibar Ltd

		Breeze Beach Club				**Veraclub Zanzibar**			
Measures	**Ratio**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**
Profitability	Gross Profit Margin	80%	76%	77%	78%	70%	71%	72%	71%
	Net Profit Margin	-6%	-24%	-13%	-14%	0.3%	1%	-1%	0.00
	EBDIT	15 %	3 %	13 %	8 %	2 %	3 %	3 %	3 %

Source:Field work

i) Gross Profit Margin

This is the excess of sales (expressed in percentage) over production costs or cost of sales. It shows by how much the amount of sales is left (after cost of sales) to absorb non production or administrative costs. Figure 23 below shows that Breeze Beach Club gross profit margin ranges between 76 percent and 80 percent while Veraclub Zanzibar ranges between 70% and 72% over the period of analysis (2008 – 2010). The room charges per pax for Breeze Beach range between USD 150 and USD 210 and for Veraclub range between USD 46 to USD 55. The direct cost of realising revenue ranges between 20% and 24% for Breeze Beach Club and 28% and 30% for Veraclub.

Taking room rate charges and direct cost into consideration, then we can conclude that Veraclub has higher production cost with lower selling price compared to Breeze Beach Club. Therefore, Breeze Beach Club has better gross profit margin than Veraclub. The gross profit margin is the indicator of the pricing policies of a hotel and its ability to control the costs. The differences in pricing strategy among hotels may cause gross profit margin and net profit margin to vary. If the average room rate per pax between these two hotels is considered, it can be seen that the rate charged by Breeze Beach Club is more than triple charged by Veraclub Zanzibar. This implies that the rate fixed by Veraclub Zanzibar is mainly to cover the running cost of the hotel. If one considers the module of business of Veraclub which deals with only one tour operator, who is the owner of the hotel, then this suggests that Veraclub may be involved in transfer pricing between the hotel and shareholder (tour operator).

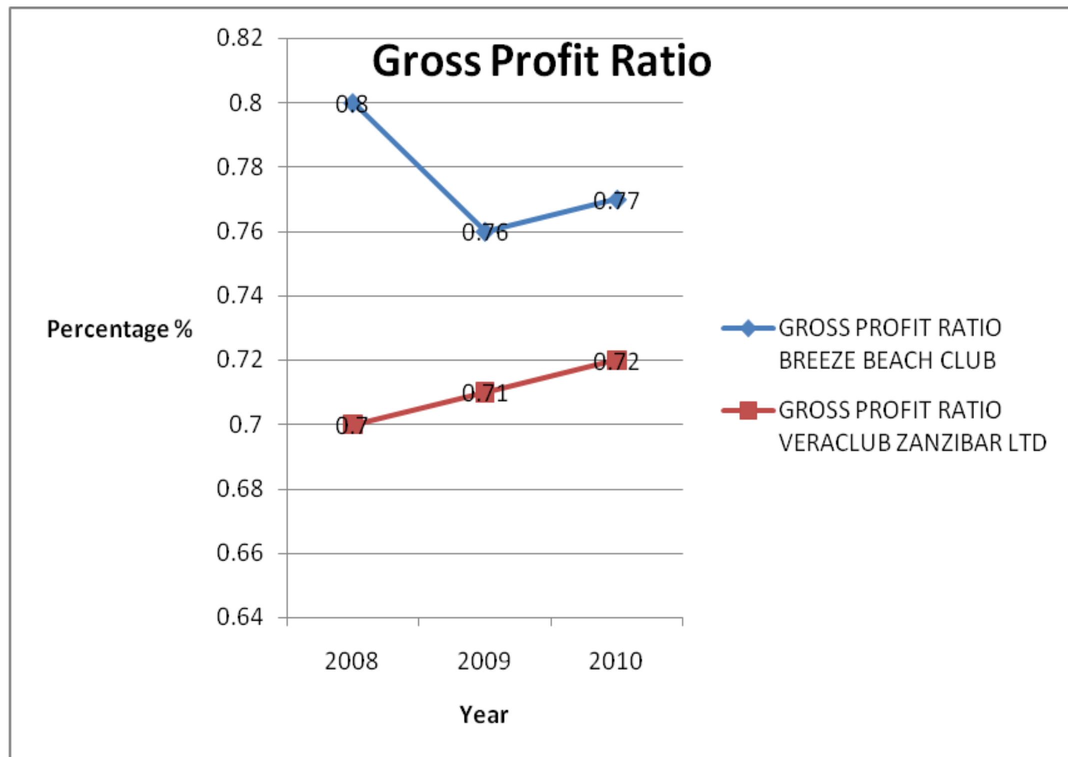

Figure 23: Gross Profit ratio between Breeze and Veraclub

Source: Field work

ii) Net Profit Margin

This shows the percentage of turnover or sales left after deducting all expenses. The ratio measures whether the hotel is efficient in controlling production and operation costs to maximize profit. Higher ratio could indicate a good sign for the management in controlling costs. The results given in figure 24 below show that Breeze Beach Club net profit ratio ranges between negative 6% and 24% while that of Veraclub ranges between negative1% and positive1% over the period of analysis (2008 to 2010). Taking this and gross profit ratio together into account, then the results suggest that despite higher production cost with lower selling price Veraclub is able to control operational expenses to maximize profit compared to Breeze Beach Club.

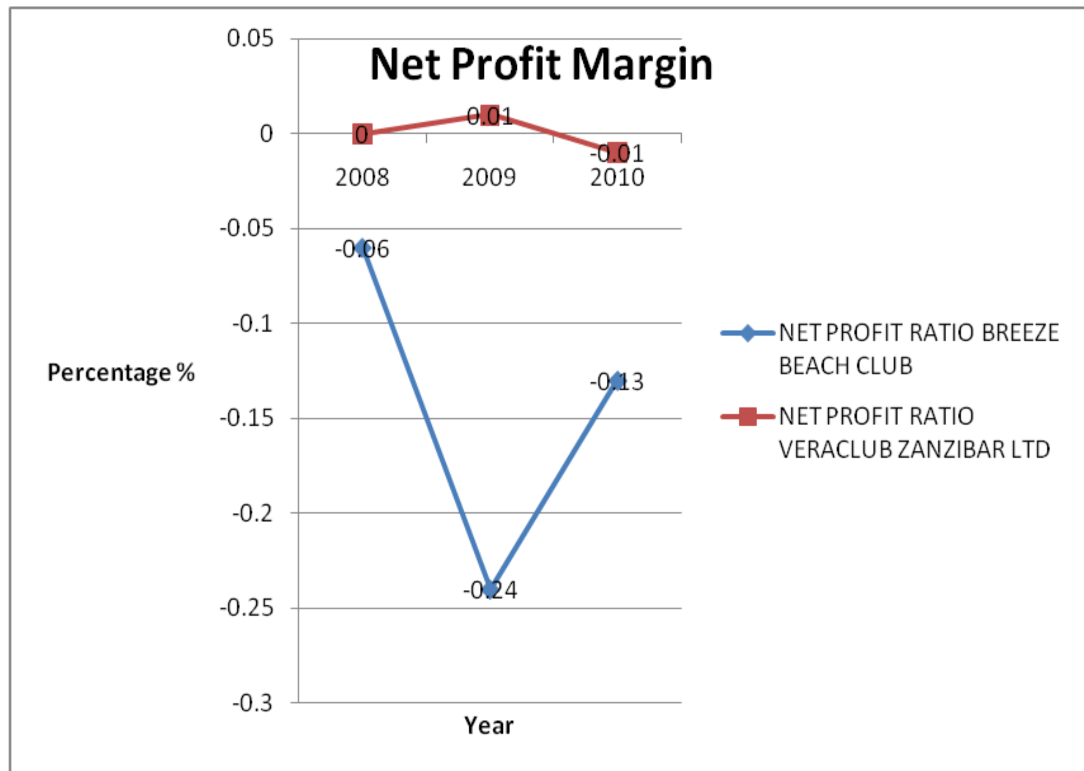

Figure 24: Net Profit ratio between Breeze and Veraclub

Source: Field work

iii) EBDIT

The analysis represented in figure 25 below indicates that Breeze Beach Club has EBDIT ratio range between 3 percent and 15 percent of the revenue while Veraclub Zanzibar Ltd ranges between 2 percent and 3 percent. The EBDIT margin is affected by more factors than the gross profit margin. The better EBDIT margin in Breeze Beach Club reflects better sales and represents image of efficient management and control of the operating costs. The EBDIT ratio is a better measure of the management's performance because it directly reflects what is under the control of management. The management has no control over the fixed charges such as depreciation, interests, and taxes.

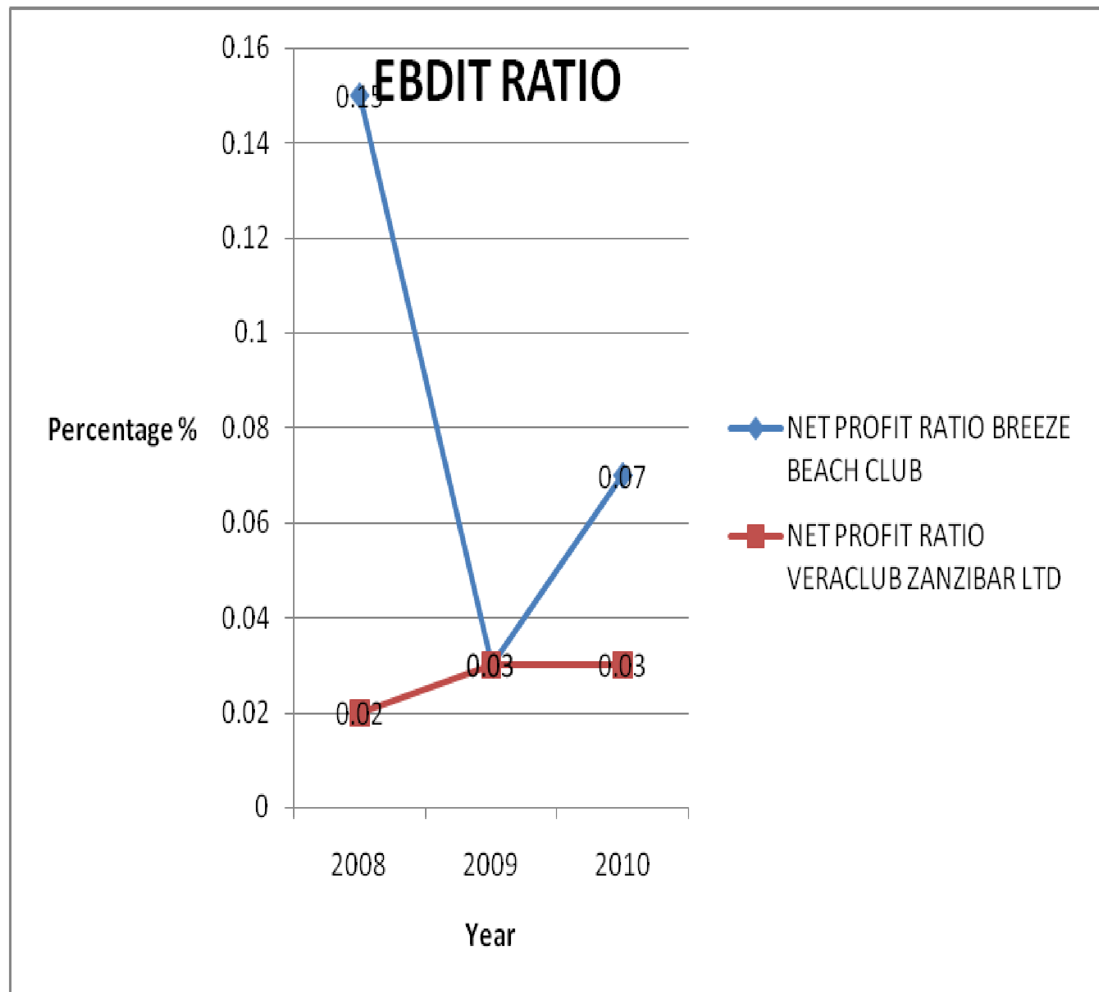

Figure 25: EBDIT Ratio between Breeze and Veraclub

Source: Field work

4.5.2 Liquidity Ratio

The liquidity ratio measures the ability of a hotel to meet its current and short term obligations. The ratios computed under this group indicate the short-term position of the hotels and also indicate the efficiency with which the working capital is being used. Commercial banks and short-term creditors may be basically interested in the ratios falling under this group. Table 16 below shows the result of liquidity of the two hotels.

Table 16: Liquidity ratios between Breeze Beach Club and Veraclub Zanzibar Ltd.

		Breeze Beach Club				Veraclub Zanzibar			
Measures	**Ratio**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**
Liquidity	Current ratio	1.16	0.57	1.08	0.94	1.09	1.15	1.0	1.08
	Quick ratio	0.93	0.49	0.95	0.79	0.95	0.99	0.94	0.96
	Cash ratio	0.38	0.08	0.6	0.35	0.17	0.06	0.05	0.09

Source:Field work

i) Current Ratio

The Current Ratio is calculated by dividing current assets by current liabilities. It is a measure of the hotel short-term solvency. Figure 26 below indicates that Breeze Beach Club has a current ratio range between 0.57 and 1.16. This means that for every dollar of current liabilities, Breeze Beach Club has an average of USD 0.57 and USD 1.16 of current assets to meet its current obligation. On other hand, Veraclub Zanzibar ltd has current ratio ranges between 1 and 1.15. This means that for every dollar of current liabilities, Veraclub has current assets between USD 1 and USD 1.15 to meet its current obligation. Therefore, based on current ratio it seems that Veraclub Zanzibar Ltd is little more sufficiently liquid compared to Breeze Beach Club.

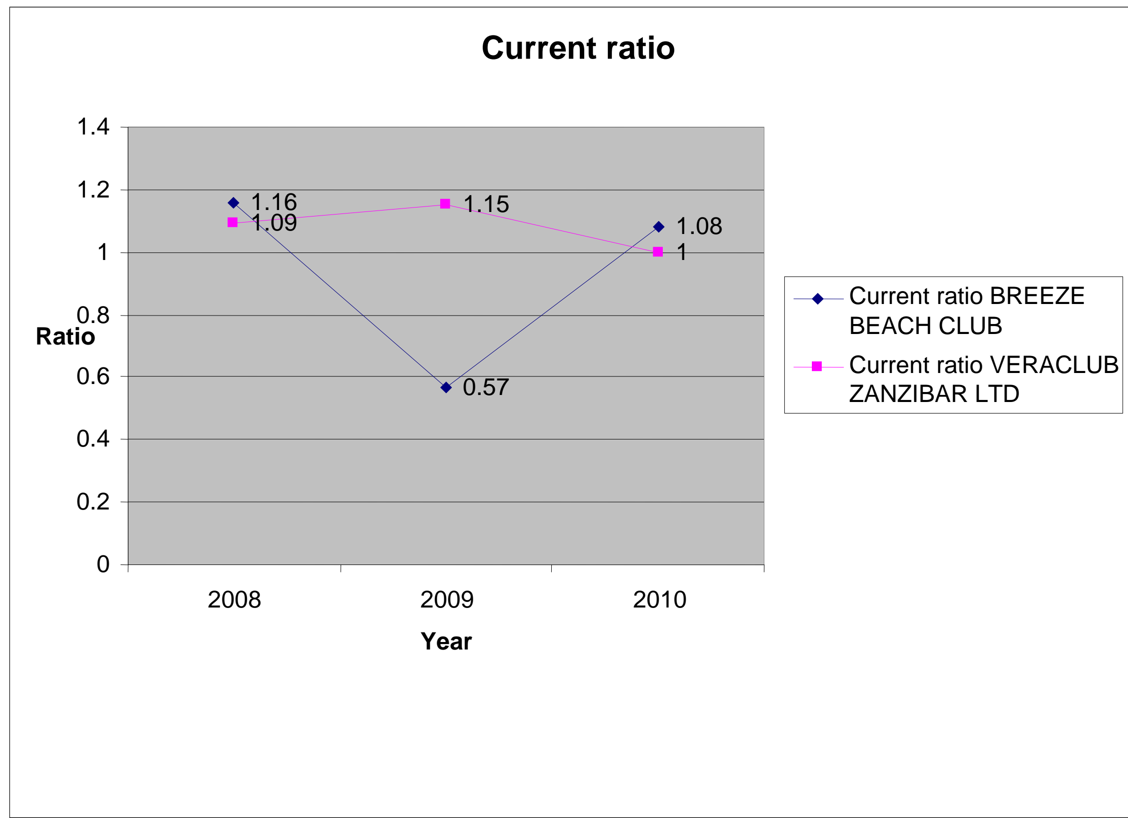

Figure 26: Current ratio between Breeze and Veraclub

Source: Field work

ii) Quick Ratio

This ratio establishes a relationship between quick or liquid assets and current liabilities. The ratio indicates the backing available to liquid liabilities in the form of liquid assets. The term liquid assets indicate the assets, which can be converted in the form of cash without any reduction in the value. Figure 27 below indicates that Breeze Beach Club has quick ratio range between 0.49 and 0.95 which is little lower compared to Veraclub Zanzibar Ltd which has quick ratio between 0.94 and 0.99. This implies that for every dollar of current liabilities Breeze Beach Club has USD 0.49 and USD 0.95 while Veraclub has USD 0.94 and USD0.99 of current assets to

meet their current obligations. The quick ratio exclude inventory from current assets because it takes time for realizing into cash. Despite the fact that Veraclub has higher quick ratio compared to Breeze Beach Club, both have little unsatisfactory current financial condition because the quick ratios for both hotels are below USD1. Thus, if the hotels' inventories do not sell, and they have to pay their entire current obligation, they may find little difficult to do that. Therefore, the hotels are slightly in danger with creditors.

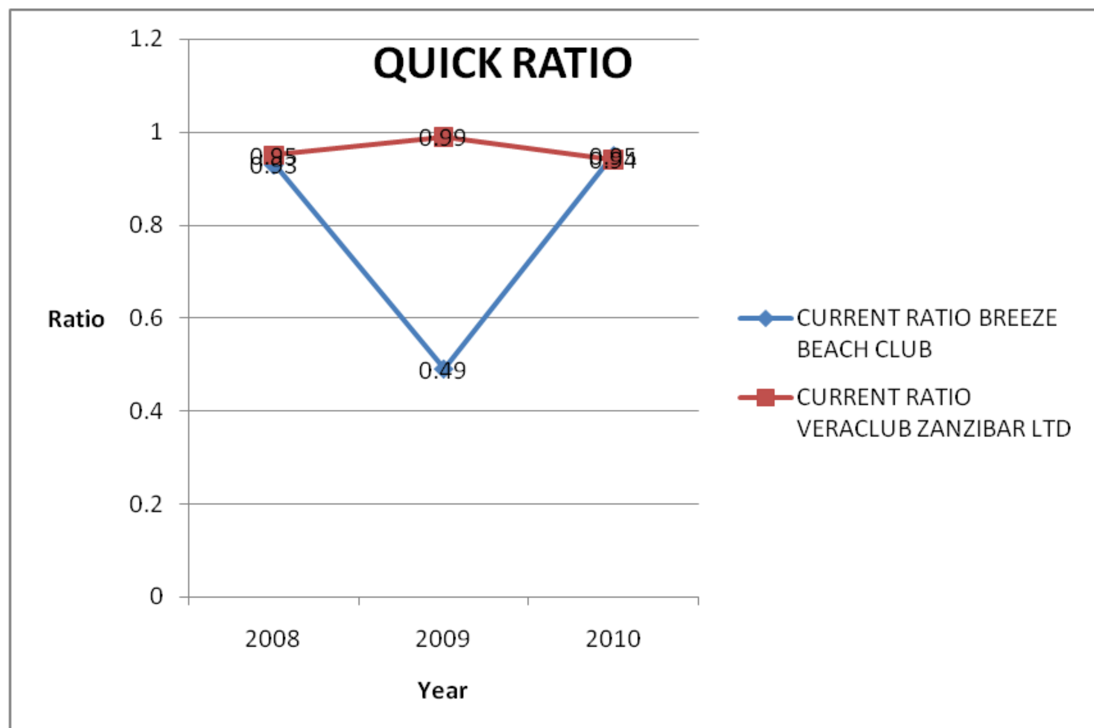

Figure 27: Quick ratio between Breeze and Veraclub

Source: Field work

iii) Cash Ratio

This ratio examines the proportion of cash and its equivalent to its current liabilities. Both hotels have low levels of cash to meet their current liabilities (see figure 28

below). However, Breeze Beach Club has better cash ratio between USD 0.08 and USD 0.6 compared to USD 0.05 and USD 0.17 of Veraclub Zanzibar. Both hotels keep low levels of cash, there is no significant risk for that if the hotels have borrowing powers. The disadvantage of maintaining low level of cash is that the hotels may miss opportunity of cash purchase. Cash purchase is cheaper compared to credit purchase; hence they are bound to reduce profit.

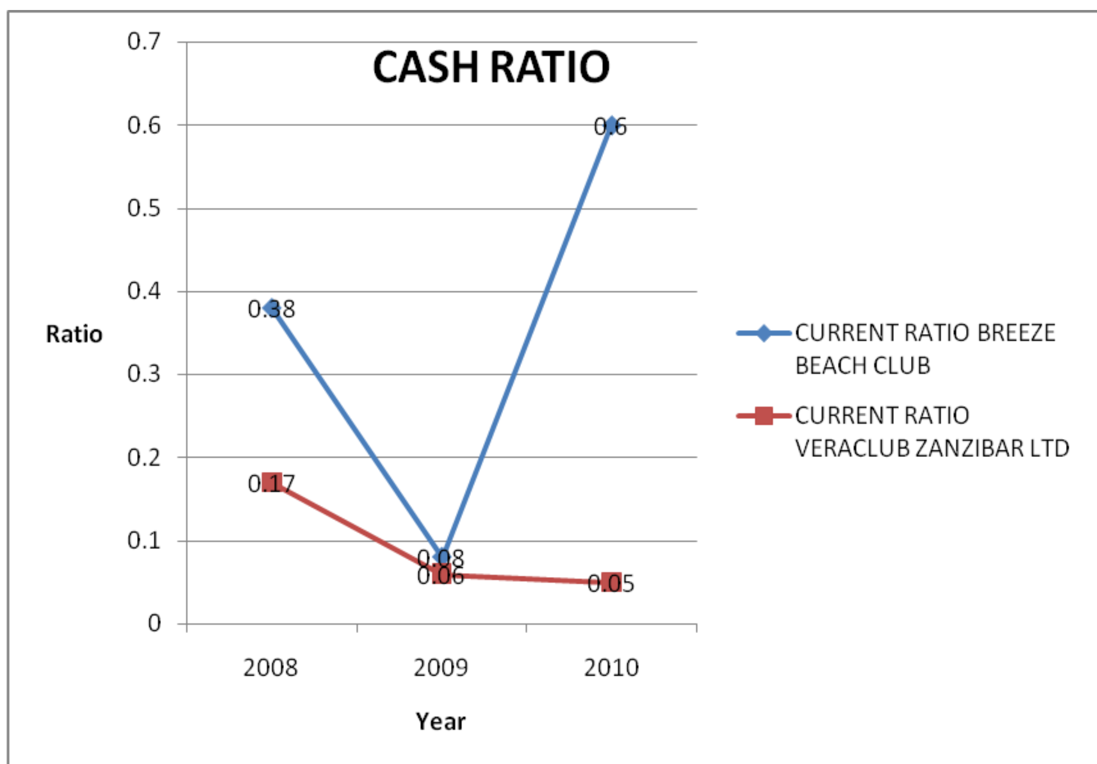

Figure 28: Cash Ratio between Breeze and Veraclub

Source: Field work

4.5.3 Activity ratio

Activity ratios are calculated to measure the efficiency with which the resources of a firm have been employed. The activity ratios are presented in table 17 below and they evaluate the efficiency with which the hotels manage and utilize their assets.

Table 17: Activity ratios between Breeze Beach Club and Veraclub Zanzibar Ltd

		BREEZE BEACH CLUB				VERACLUB ZANZIBAR			
Measures	**Ratio**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**
Activity	Inventory turnover	1.62	2.05	2.88	2.18	2.90	3.02	2.85	2.92
	Debtors turnover	14.74	10.60	18.29	14.54	8.06	9.30	3.02	6.79
	Total assets turnover	1.08	0.87	1.10	1.02	4.19	4.87	1.99	3.68

Source:Field work

i) Inventory Turnover

It is calculated by dividing the cost of goods sold by the average inventory. The ratio is used to measure the efficiency of the hotel in selling its product. The inventory turnover shows how rapidly the inventory is turning into receivable through sales. Generally, a high inventory turnover is indicative of good inventory management. Figure 29 below indicates that Breezes Beach Club inventory turnover's ranges

between 1.62 times and 2.88 times for the period under analysis (2008-2010). In other words, the hotel holds average inventory of between 12 months/2.88 and 12 months/1.62 which is equivalent to 4.2 months 7.4 months respectively. On other hand Veraclub Zanzibar holds average inventory between 12 months/3.02 and 12 months/2.85 which is equivalent to 3.97 months and 4.2 months respectively. This shows that Veraclub Zanzibar has good inventory management compared to the Breeze Beach Club. The results also suggest that the Veraclub Zanzibar was faster to turn inventories into receivables through sales.

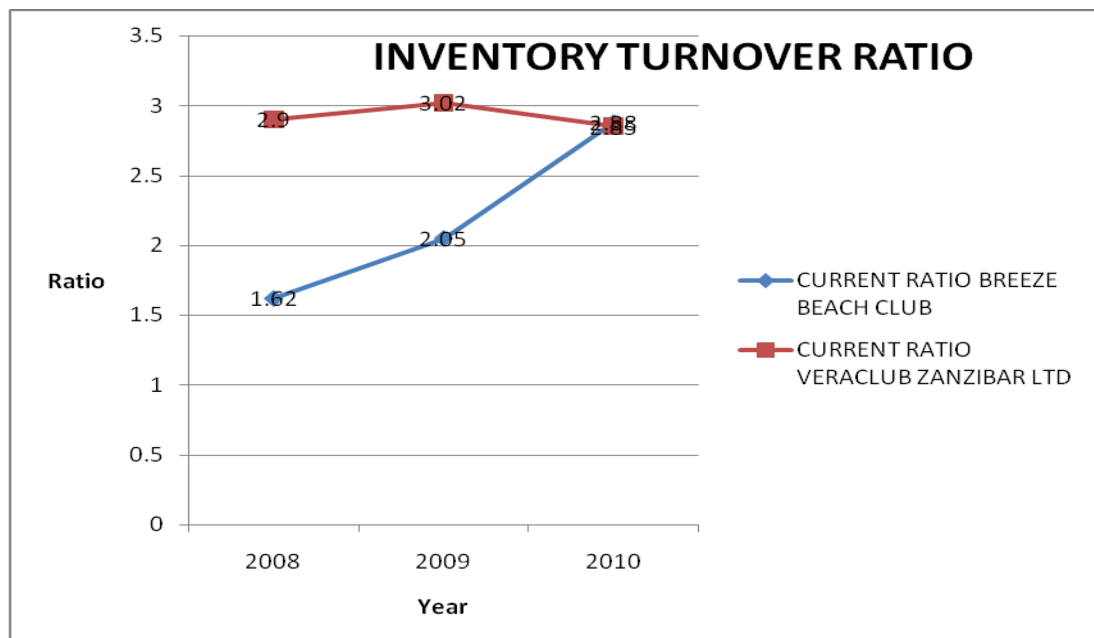

Figure 29: Inventory turnover ratio between Breeze and Veraclub

Source: Field work

ii) Debtors Turnover

Debtors turnover indicates the number of times debtors turn over each year. Generally the higher the value of debtors turnover, the more efficient is the management of credit. Figure 30 below indicates that debtors turnover of Breeze

Beach Club ranges between 10.6 times and 18.29 times for the period under analysis (2008 to 2010). In other words, the book debts of the hotel remain unpaid for a period between 12 months/18.29 and 12 months/10.6 which is equivalent to 0.66 months and 1.13 months respectively. On other hand, the debtor's turnover of Veraclub Zanzibar ranges between 3.02 times to 9.3 times. This is equivalent to 1.3 months (12 months/ 9.3) and 4 months (12 months/3.02).

These findings show that, debtors turnover of Breeze Beach Club is more than two times higher than Veraclub Zanzibar. In business terms, Breeze Beach Club is faster in collecting its receivable, and thus has stronger liquidity when compared to Veraclub Zanzibar. The situation means that Breeze Beach Club has a lower risk of bad debts due to faster cash collection compared to Veraclub Zanzibar.

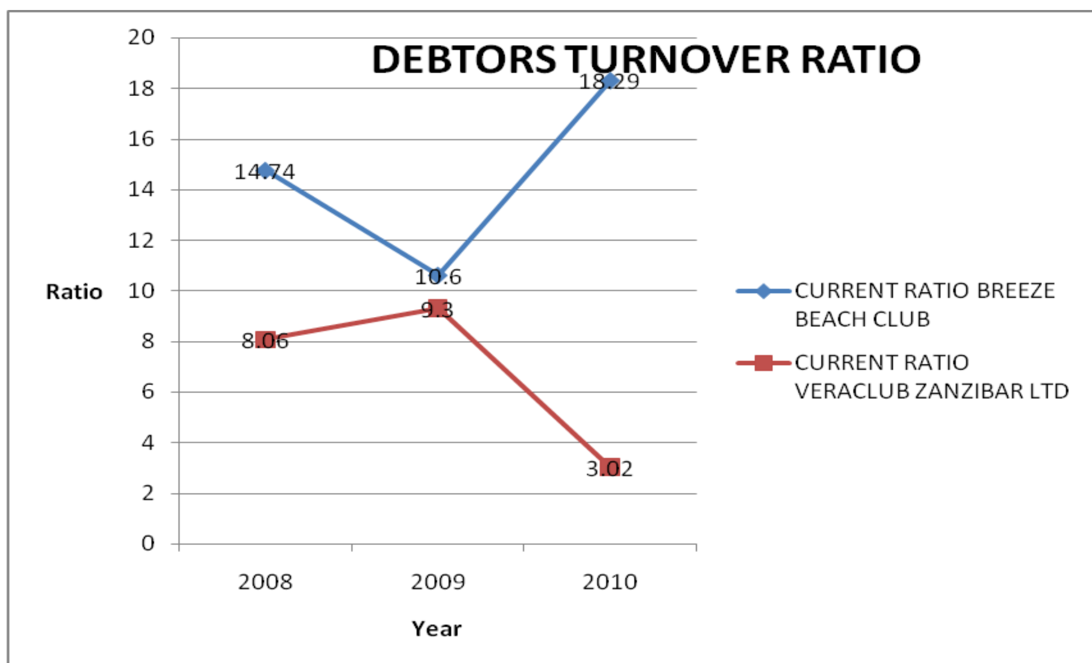

Figure 30: Debtors turnover ratio between Breeze and Veraclub

Source: Field work

iii) Total Assets Turnover

This ratio measures the efficiency in assets utilization; it shows to what extent hotel's assets are utilized to generate revenue. The results of analysis as shown in figure 31 below indicates that Breeze Beach Hotel generates between USD 0.87 and USD1.10 in sales or revenue for every dollar of total assets (net fixed assets plus current assets). On other hand, Veraclub Zanzibar generates between USD 1.99 and USD 4.87 for every dollar invested in fixed assets and current assets together for the period under analysis (2008 to 2010). The total assets turnover ratio shows that there is a big difference between the hotels in utilizing the assets.

The difference is expected because Veraclub does not own its hotel buildings and contents which results in low fixed assets compared to Breeze Beach Club. Veraclub Zanzibar Ltd is utilizing fixed assets (example land and building, plant and machinery) of the hotel's landlord to generate revenue.

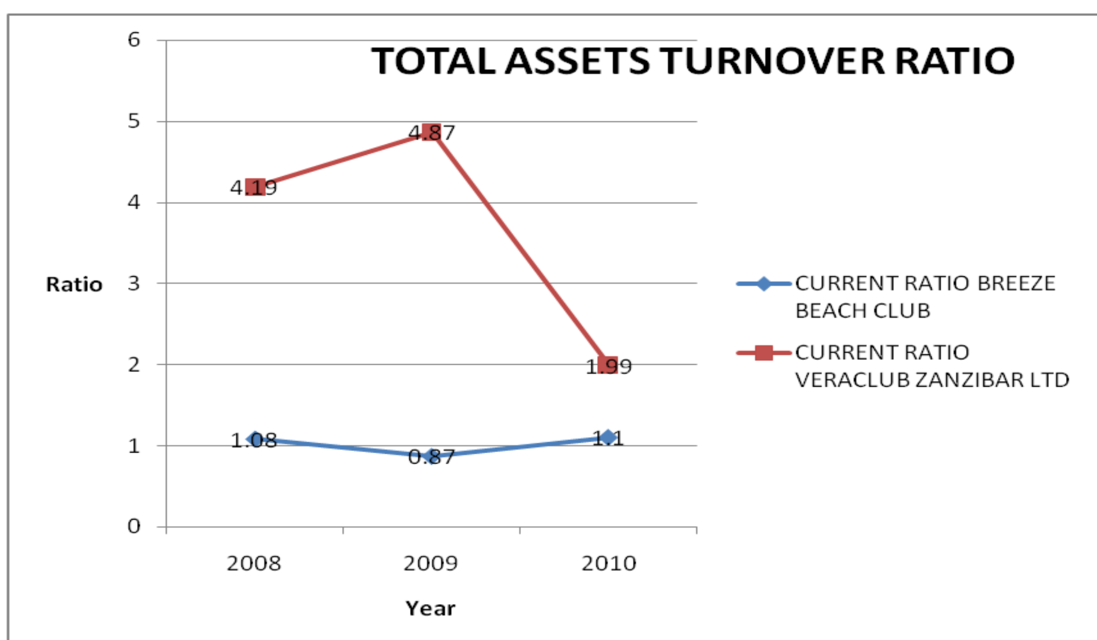

Figure 31: Total assets turnover ratio between Breeze and Veraclub

Source: Field work

4.5.4 Leverage Ratio

Leverage ratios indicate mix of funds provided by owners and outsiders (lenders). The ratio provides measures of the firm's use of debt financing. Table 18 below shows the leverage ratio between two hotels.

Table 18: Leverage ratios between Breeze Beach Club and Veraclub Zanzibar Ltd

		Breeze Beach Club				Veraclub Zanzibar			
Measures	**Ratio**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**	**Year 2008**	**Year 2009**	**Year 2010**	**Average**
Leverage	Debt Ratio	1.06	1.28	1.41	1.25	0.75	0.67	0.89	0.77
	Debt-equity	(16.60)	(4.53)	(3.46)	-8.20	3.05	2.06	7.83	4.31

Source:Field work

i) Debt Ratio

Debt ratio is a measure of the financial stability of a company; it is a common mode of evaluation for any investment which requires a loan. The lower the company's reliance on debt for asset formation, the less risky the company is. On the other hand,

the higher ratio means a company has high insolvent risk since excessive debt can lead to a heavy debt repayment burden.

The debt ratio of Breeze Beach Club shows that external funds range between 1.06 times and 1.41 times for the period of analysis (2008 to 2010). This means that the hotel debt is between USD1.06 to USD 1.41 for every dollar of assets. In other words, outsiders contribute between USD 1.06 and USD 1.41 for every dollar of its assets. This is higher reliance on debt which is risky and may lead to insolvency.
On the other side, debt ratio of Veraclub Zanzibar shows that outsiders contribute between 67 percent and 89 percent of its assets with external fund. It is clear that Breeze Beach Club relies more on debt to finance its assets compared to Veraclub Zanzibar. This implies that Breeze Beach Club claims from creditors (outsiders) are greater than those of owners. A high level of debt brings in inflexibility in the firm's operations due to the increasing interference and pressures from outsiders. Therefore, based on debt ratio analysis, Veraclub Zanzibar is healthier than Breeze Beach Club. Figure 32 below represents results of debt ratio between Breeze Beach Club and Veraclub Zanzibar Ltd.

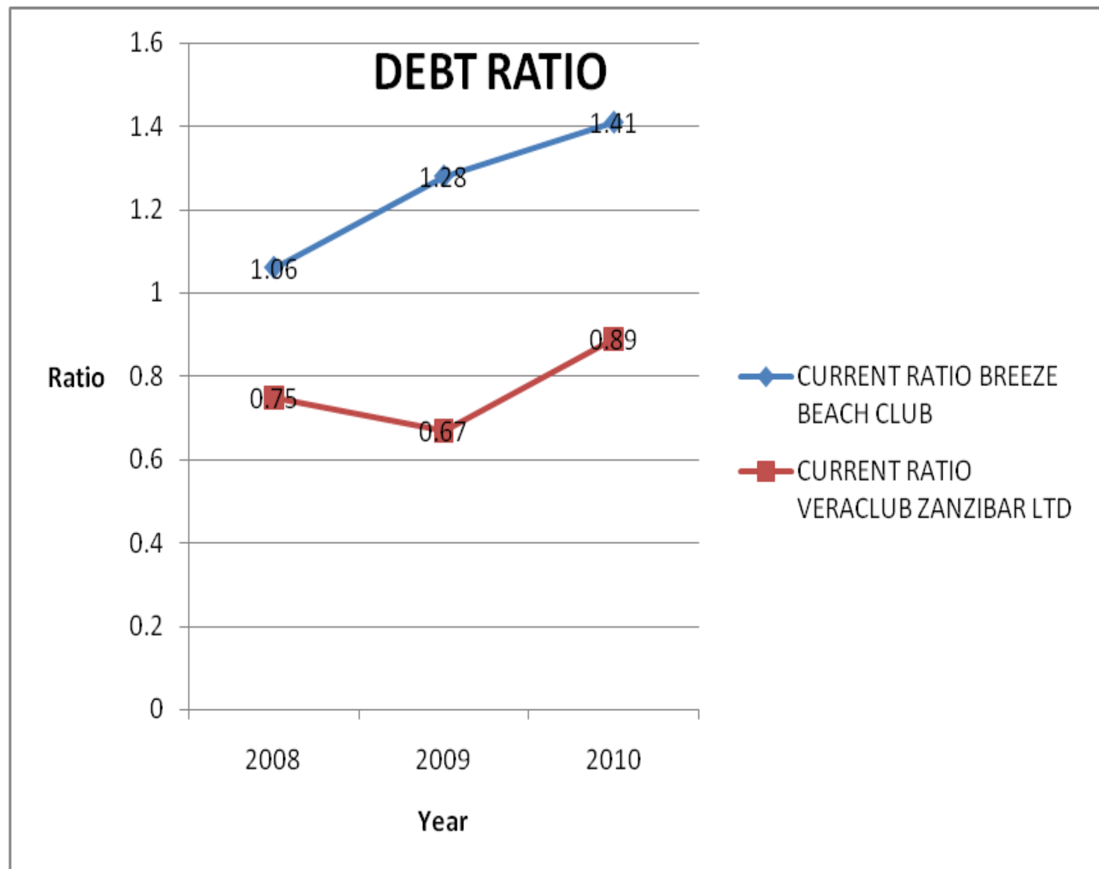

Figure32: Debt ratio between Breeze and Veraclub

Source: Field work

ii) Debt-equity

Debt-to-Equity ratio indicates the relationship between the external equities or outsiders funds and the internal equities or shareholders funds. It is also known as external-internal equity ratio. It is determined to ascertain soundness of the long term financial policies of the company. A high debt to equity ratio could indicate that the company may be overleveraged; meaning a customer is overly reliant on debt as a source of financing. Figure 33 below indicates that Breeze Beach Club has debt-equity ratio between negative 16.60 and negative 3.46 for the period under analysis (2008 to 2010).

This means that the lenders contribution range between USD 3.46 and USD 16.60 for every negative dollar of owners' contributions. The negative equity of Breeze Beach hotel is a result of excessive previous losses the hotel suffers. This means that owners of the Breeze Beach Club have nothing to claim against hotel's assets because the claims from outsiders are higher than all assets of the hotel and the owners are normally the last one to be paid in case of liquidation. These findings concur with those on Debt Ratio. On other hand, Veraclub Zanzibar has debt-equity ratio range between 2.06 and 7.83 for the period under analysis (2008 to 2010). This implies that for every dollar of owners' contribution, outsiders contribute between USD 2.06 and USD 7.83. This means that the hotel depends on outsiders especially on creditors to finance their operations. The analysis shows that in one way or another both hotels depend on outsiders to finance their operations. However, Breeze Beach Club is heavily relying on external source to finance its operation compared to Veraclub Zanzibar.

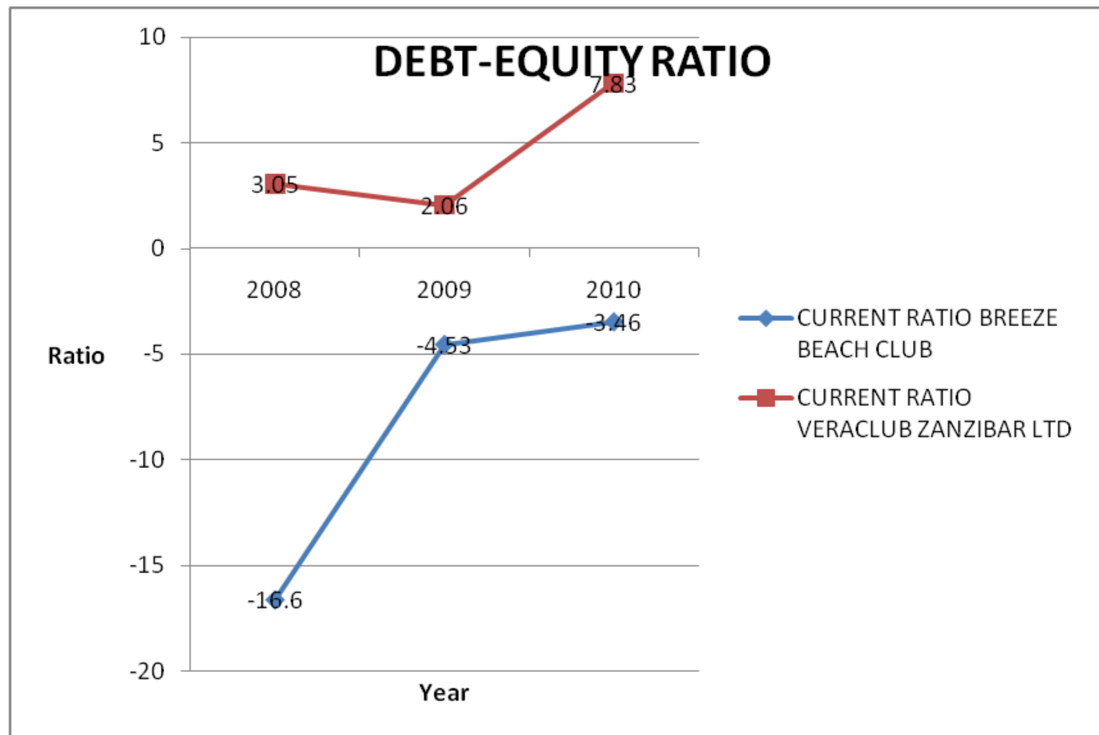

Figure 33: Debt -Equity ratio between Breeze and Veraclub

Source: Field work

CHAPTER FIVE

5.0 CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

As highlighted in chapter one, the objective of this research is to determine the financial conditions and performances of two hotels, one known as Package hotel (All-inclusive “club”) and second one is Non Package hotel. The study focused on financial ratios to analyse the profitability, liquidity, solvency, and efficiency of using assets productively among the type of hotels. The outcomes of this analysis show how healthy are these hotels and which hotel is healthier than the other.

Analysis and comparable study of financial statements is a task performed by different groups such as management, lenders and investors. The methods, techniques and variables to be applied in the analysis will differ depending on the analyst interests, though all may use the financial statements. Ratios used in this analysis are not all applied by different groups to analyse efficiency, profitability, liquidity and solvency of the hotel industry. However, the selected ratios are very common in the field of financial analysis and are very useful to different stakeholders who wish to make sound economic decisions.

Based on research findings on Chapter Four of this study, it is appropriate to conclude that both hotels faced different levels of return, risk, and efficiency in using their assets productively. In observing gross profit margin, net profit margin and EBDIT ratios to determine profitability of individual and comparable hotels, it was

found that most of the ratios are not favourable. For instance, the net profit margin (NP) of Breeze Beach Club for all years under analysis averaged negative 14 percent. This signified that the performance of the hotel was not good during this period.

On other hand, Veraclub Zanzibar Ltd has average of zero percent net profit margin. This as well signifies low performance of Package hotel (Vera Zanzibar). However, if these hotels are compared from each other, the results show that Veraclub hotel has good return compared to Breeze Beach Club. Interested groups such as management, creditors and investors will be very concerned on this low performance of the hotels. However, they should consider other economic factors such as crisis and power black out that took place in 2009 and 2010. All these were the challenges that affected the whole hotel industry.

In observing current, quick and cash ratios to determine liquidity of the hotel, then the conclusion is that the Non Package hotel (Breeze Beach Club) has low liquidity. On average, all ratios computed to measure liquidity of Breeze Beach Club were below 1. This implies that the hotel has been facing difficulties to meet its current obligation. If the situation is observed from another angle, Veraclub current ratio's on average was more than 1, the quick ratio was very close to 1, except for cash ratio which below 0.5. In general, the current assets of Veraclub Zanzibar are more than current liabilities which represent better liquidity and less risky business environment. The conclusion is clear that, Veraclub Zanzibar has good financial position which can meet its current obligations. Despite the conclusions that show Breeze Beach Club to have low liquidity compared to Veraclub Zanzibar, but the

hotel did not get any pressure from creditors to demand immediate payments. This is due to good and long term relationship between the hotel and suppliers. In this sense, creditors and short tem lenders should not only consider liquidity ratios but they should consider other factors such as commitment and responsibility to handle outsiders claims.

Looking at leverage ratios to determine the extent to which debt is used in capital structure of the hotels, the conclusion drawn therein is that Breeze Beach Club is overleveraged. This means that the hotel is heavily relying on debt as a source of finance rather than using retained earnings to finance its business. For instance, an average debt of Breeze Beach Club is USD 1.25 for every dollar of its assets. The capital structure of the Breeze Beach Club also concludes that external equities are more than internal equities.

On other hand, debt ratio of Veraclub Zanzibar is below USD1. This signifies that the hotel has more assets than liabilities. The conclusion here is that the Breeze Beach Club is operating at higher risk compared to Veraclub Zanzibar. In short Veraclub Zanzibar may appear to be less risky than the Breeze Beach Club. However, there are also other factors apart from financial ratios which can put the hotel in risky. For example, the Income Tax Act 2004 section 34(1) state that 'where a person attempts to split income with another person, the Commissioner may, by notice in writing adjust amounts to be included or deducted in calculating the income of each person '. In this case if Veraclub could not provide evidence to Commissioner of Income Tax that the rate charged to tour operator (shareholder of

Vera) is at arm's length, then the Commissioner may accuse the hotel for fixing lower rate purposely as a means of transfer pricing(split income) between the hotel and tour operator abroad. Therefore, when the Commissioner may not be convinced with the rate charged by Veraclub and hence ask the management to revise the rate which will then cause more tax burden.

Veraclub Hotel is also in a high risk of failure because of its high reliance on a single tour operator to supply guests. In case the tour operator becomes bankrupt then definitely, the hotel will suffer or fail in its business. If one considers these and other factors, apart from financial ratios, it can be concluded that Veraclub Zanzibar is also at risk. In this situation, the long-term creditors, lenders, and investors should be very careful on to judge the long-term solvency of the hotel.

In observing efficiency of hotel in selling its product, the conclusion is that Veraclub Zanzibar has quick turn inventory into sales compared to Breeze Beach Club. This signifies how efficient the management of Veraclub in controlling its inventory is. Looking at how faster the hotel is turning receivable into cash, the conclusion is that the Breeze Beach Club is faster than Veraclub. The assets turnover ratios conclude that Veraclub Zanzibar is effectively utilizing its assets to generate revenue compared to Breeze Beach Club.

In general, the results in chapter four and conclusion above show that there is no way that one ratio can be used to judge profitability, liquidity, efficiency or solvency of the hotel. For effective financial analysis, the analyst should use several financial and

non financial ratios together with other laws and regulations relate to environment in which the business exists.

5.2 Recommendation

5.2.1 To the Management

Referring to the two hotels analysed, despite challenges faced, there are also opportunities to improve their efficiency or reduce risk. For example, Breeze Beach Club has huge foreign and local debts that cause poor performance and weak financial health. Foreign debts raised forex exchange loss every year that reduced profitability of the hotel. It is recommended that the hotel should apply hedging techniques such as entering into future contract or to negotiate with borrowers to pay in Tanzania Shilling instead of paying foreign currency. By doing this then the forex exchange loss may be reduced. The hotel can also negotiate with debtors to convert their debt into Share Capital. However, this will attract additional cost of 1.1 percent of the amount convert to share capital as a cost of increase share capital. Any techniques to hedge currency exposure need to be applied careful.

On other hand, Veraclub Zanzibar can improve its profitability if it can negotiate with tour operator to increase bed night rate at least to USD 100. However, this also will attract to pay more hotel levy to Zanzibar Revenue Board. The hotel can also change its marketing strategies to allow dealing with more than one tour operators. This will improve going concern of the hotel and reduce risk of depend on one tour operator.

5.2.2 To the Government

Because of its importance of comparable financial analysis, it is recommended that the Government should establish a division under Zanzibar Commission for Tourism or under any Government agency which will provide statistical data (example hotel industry average ratios) which can be used as a benchmark for comparison among the hotels.

5.2.3 Areas for further study

This study has analyzed and compared two financial statements of the hotels identified as Package and Non Package hotels. The results represent those individual hotels and not as a group or type of hotel. In this regards, this study leaves other areas for further studies such as an in depth research on financial performance of Packages and Non Packages hotels in Zanzibar. Another with studying is on benchmarking financial ratios for hotels in Zanzibar.

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APPENDICIES

APPENDIX I: Questionnaires

Introduction

The researcher is a student of The Open University of Tanzania (OUT), studying Master Degree in Business Administration (MBA). You are kindly requested to answer the questions below. In this way you will assist the researcher in accomplishing his academic requirement for field experience and research. Information collected through this questionnaire shall be treated as confidential and purposely for academic achievement. Please fill all boxes below:-

1. How many rooms available in your hotel for each of the following years?

2008	2009	2010

2. Total number of guests for each of the following years.

2008	2009	2010

3. What is the average room rate per pax for each of the following years?(Use USD only)

2008	2009	2010

4. What is the number of trade debtor at the end of each of the years? (Use USD only)

2008	2009	2010

5. a) Are there any long-term foreign debts the company is obliged to pay?

    i. Yes ☐

    ii No ☐

    b) If “Yes” how much for each in the following years? (use USD only)

2008	2009	2010

    c) Does the Company take any measures to minimise risk on foreign loan due to exchange rates fluctuation?

    i Yes ☐

    Ii No ☐

If “Yes” What are the measures

----

5. How long have you been doing a business with your big suppliers?(Please tick in appropriate box below)

   a) 1 to 2 years □

   b) 3 to 5 years □

   c) More than 5 years □

6. Is there any year the suppliers demand cash payment instead of credit?

   i Yes □ □

   ii No □ □

   If "Yes" Which year?

APPENDIX II

Financial Statements for Breezes Beach Club

Nova Hotels Limited (Breezes Beach Club)

Statement Of Financial Position

	USD	USD	USD
ASSETS	**2008**	**2009**	**2010**
Non currents assets			
Property, plant and equipment.	3,083,237.75	2,898,892.91	2,454,832.35
Currents Assets			
Other receivables	12,658.40	15,967.11	33,225.01
Trade Debtors	269,146.41	269,804.36	188,573.56
Stocks	114,772.34	55,785.27	82,041.58
Cash and cash equivalent	191,108.06	55,899.16	381,644.19
	587,685.20	397,455.90	685,484.34
TOTAL ASSETS	**3,670,922.95**	**3,296,348.82**	**3,140,316.69**
EQUITY AND LIABILITY			
Capital and reserves			
Share capital	390,625.00	390,625.00	390,625.00
Retained Earnings	(625,985.21)	(1,323,727.28)	(1,667,820.67)

Total Capital and Reserves	**(235,360.21)**	**(933,102.28)**	**(1,277,195.67)**
Non -current liability			
Long term Loans	1,034,617.42	1,227,558.87	1,702,317.32
Shareholders' advance	2,364,167.31	2,304,748.02	2,081,247.70
	3,398,784.73	3,532,306.90	3,783,565.02
Current liabilities			
Trade creditor and accruals	507,498.43	697,144.20	633,947.34
Total liabilities	**3,906,283.16**	**4,229,451.09**	**4,417,512.36**
TOTAL EQUITY AND LIABILITIES	**3,670,922.95**	**3,296,348.81**	**3,140,316.69**

Nova Hotels Limited (Breezes Beach Club)
Statement of Comprehensive Income

	USD 2008	**USD 2009**	**USD 2010**
Revenue	3,966,486.53	2,860,561.33	3,449,145.37
Cost of Sales	783,592.64	697,609.81	793,455.41
Gross Profit	3,182,893.89	2,162,951.52	2,655,689.96
Operating cost	2,603,158.52	2,075,794.99	2,397,278.60
EBDIT	579,735.37	87,156.53	258,411.37
Depreciation	200,222.59	242,668.37	204,365.70
Interest	551,408.78	497,477.11	488,625.60
Tax	50,300.46	28,113.90	-
Profit/(Loss)	**(222,196.46)**	**(681,102.85)**	**(434,579.93)**

APPENDIX III:

Financial Statements for Veraclub Zanzibar Ltd

Veraclub Zanzibar Ltd
Statement of Financial Position

	USD 2008	USD 2009	USD 2010
ASSETS			
Non currents assets			
Property, plant and equipment.	72,145.03	78,649.30	100,638.73
Currents Assets			
Other receivables	26,631.48	35,394.86	115,439.02
Trade Debtors	210,262.81	179,956.00	594,317.12
Stocks	43,149.87	36,294.17	53,194.39
Cash and cash equivalent	51,833.85	13,396.07	38,699.86
	331,878.01	**265,041.10**	**801,650.39**
TOTAL ASSETS	**404,023.04**	**343,690.40**	**902,289.12**
Equity and Liability			
Capital and reserves			
Share capital	3,076.92	3,076.92	3,076.92
Retained Earnings	96,687.66	109,170.92	99,146.54
Total Capital and Reserves	**99,764.58**	**112,247.84**	**102,223.46**
			Non current liability
Long term Loans	-	-	-
Current liabilities			
Trade creditor and accruals	304,258.46	231,442.56	800,065.65
Total liabilities	**304,258.46**	**231,442.56**	**800,065.65**
Total Equity and Liabilities	**404,023.04**	**343,690.40**	**902,289.11**

Veraclub Zanzibar LTD			
	USD	USD	USD
	2008	**2009**	**2010**
Revenue	1,694,045.46	1,674,030.00	1,794,119.82
Cost of Sales	505,702.62	479,305.82	509,268.09
Gross Profit	1,188,342.84	1,194,724.18	1,284,851.73
Operating cost	1,146,202.51	1,140,292.98	1,238,342.53
EBDIT	42,140.33	54,431.20	46,509.20
Depreciation	25,320.00	31,947.94	48,187.20
Tax	11,616.84	10,800.00	9,847.47
Profit/(Loss)	**5,203.49**	**11,683.26**	**(11,525.47)**

Appendix IV:

Financial Ratios of Breeze Beach Club

Measure	Ratios	**2008**	**2009**	**2010**	**AVERAGE**
Profitability	Gross Profit Margin	0.80	0.76	0.77	0.78
	Net Profit Margin	-0.06	-0.24	-0.13	-0.14
	EBDIT	0.15	0.03	0.07	0.08
Liquidity	Current Ratio	1.16	0.57	1.08	0.94
	Quick Ratio	0.93	0.49	0.95	0.79
	Cash Ratio	0.38	0.08	0.60	0.35
Activity	Inventory turnover	1.62	2.05	2.88	2.18
	Debtors turnover	14.74	10.60	18.29	14.54
	Total assets turnover	1.08	0.87	1.10	1.02
Leverage	Debt ratio	1.06	1.28	1.41	1.25
	Debt-equity	-16.60	-4.53	-3.46	-8.20

Appendix V
Financial Ratios Of Veraclub Zanzibar Ltd

Measure	Ratios	**2008**	**2009**	**2010**	**AVERAGE**
Profitability	Gross Profit Margin	0.70	0.71	0.72	0.71
	Net Profit Margin	0.003	0.01	-0.01	0.00
	EBDIT	0.02	0.03	0.03	0.03
Liquidity	Current Ratio	1.09	1.15	1.00	1.08
	Quick Ratio	0.95	0.99	0.94	0.96
	Cash Ratio	0.17	0.06	0.05	0.09
Activity	Inventory turnover	2.90	3.02	2.85	2.92
	Debtors turnover	8.06	9.30	3.02	6.79
	Total assets turnover	4.19	4.87	1.99	3.68
Leverage	Debt ratio	0.75	0.67	0.89	0.77
	Debt-equity	3.05	2.06	7.83	4.31

APPENDIX VI:

About Breeze Beach Club

BBC is hotel conduct its business in East coast in the Island of Unguja (Zanzibar). The hotel established in 1997 and operates with 74 rooms. The hotel provides accommodation and catering services. It has employed more than 330 workers. The main market of the hotel is Europe and America. The hotel deals with several tours operators who get commission for supplies of guests. It also gets direct guests from different destinations around continents. The hotel classified as a Non Package hotel.

APPENDIX VII

About Veraclub Zanzibar

Veraclub is a company that runs hotel business in the Island of Unguja (Zanzibar). The Company established in 1998 and operates with 76 rooms. It provides accommodation and catering services. The hotel has employed more than 255 employees into different departments. The hotel focuses on Europe market particular in Italy. It has sole tour operator who supplies guest and also is a shareholder of the hotel. The hotel classifies as a Package hotel or popular known as All-Inclusive "club".